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In The

Supreme Court of the United States

October Term, 1995

CORNISH SHIPPING LTD.,

Petitioner,

vs.

INTERNATIONAL NEDERLANDEN BANK N.V., f/k/a NMB POSTBANK GROEP, N.V.,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the method by which a shipowner enforces its maritime lien on subfreights should now be changed from the traditional *in rem* action against the fund itself (*i.e.*, an arrest of the *res*), to essentially an *in personam* action which can only be pursued against the payor.

2. Whether a shipowner's superior maritime lien on subfreights can be defeated by the actions of an inferior land based secured party, who manipulates or interferes in the transfer of the *res*, and then seeks to retain that *res* on the basis that "payment" under any circumstance extinguishes the shipowner's lien.

PARTIES TO THE PROCEEDING AND RULE 29.1 STATEMENT

In addition to Petitioner Cornish Shipping Ltd. and Respondent International Nederlanden Bank N.V., f/k/a NMB Postbank Groep N.V., Pohang Iron & Steel Co., Ltd. was an appellant in the Court of Appeals.

There are no parent or subsidiary companies of Petitioner Cornish Shipping Ltd.

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Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITION FOR WRIT OF CERTIORARI

Cornish Shipping Ltd. respectfully petitions for a Writ of Certiorari to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered on April 20, 1995.

OPINIONS BELOW

The decision of the Court of Appeals of which review is sought was entered on April 20, 1995, and is reported at 53 F.3d 499 (2d Cir. 1995) (App. 1a-19a).[1] The opinion of the District Court is reported at 1995 AMC 235 (S.D.N.Y. 1994) (App. 20a-34a).

STATEMENT OF JURISDICTION

The judgment of the Court of Appeals was entered on April 20, 1995. A Petition of Writ of Certiorari is due on July 19, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

TREATIES AND STATUTES INVOLVED

This case involves the enforcement of a maritime lien on subfreights, as implemented under the Supplemental Rules for Certain Admiralty and Maritime Claims, including Rule C, which provides in relevant part:

> Rule C. Actions *in Rem:* Special Provisions
>
> (1) When Available. An action *in rem* may be brought:
>
> (a) To enforce any maritime lien; . . .
>
> (3) Judicial Authorization and Process.
>
> . . . If the property that is the subject of the action consists in whole or in part of

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1. References to the Appendix are cited as "App. __a".

> freight, or the proceeds of property sold, or other intangible property, the clerk shall issue a summons directing any person having control of the funds to show cause why they should not be paid into court to abide the judgment.

STATEMENT OF CASE

A. District Court Jurisdiction

Jurisdiction of the United States District Court, Southern District of New York, was based upon that Court's admiralty and maritime jurisdiction under 28 U.S.C. §1333(1).

B. Factual Background/Procedural History

The facts of this case are not complicated — they involve competing claims by a shipowner and a bank to a single subfreight fund of approximately $1.6 million. The result in the Court below, however, was extraordinary.

The Petitioner Cornish Shipping Ltd. ("Cornish") chartered its vessel to Ferromet Resources, Inc. ("Ferromet") under a New York Produce Exchange ("NYPE") form charter party which provided Cornish with a lien on subfreights.[2] The charterer Ferromet defaulted under the charter. The owner Cornish then exercised its charter party lien on the subfreights by, *inter alia,* filing an *in rem* action in the Southern District of New York. The arrest warrant specified a seizure of the subfreights to be paid to the charterer Ferromet, and was served on the charterer's bank, International Nederlanden Bank N.V. ("INB").

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2. Subfreights denote the freight payment made by a third party (including a sub-charterer, shipper or consignee) to the charterer for the ocean transportation of the cargo (App. 3a).

Previously, the cargo receiver Pohang Iron & Steel Co. Ltd. ("POSCO") had arranged for payment to Ferromet through a letter of credit which POSCO opened at the Shinhan Bank ("Shinhan L/C"). Ferromet's contract of sale with POSCO was on CIF terms — thus, the proceeds under the Shinhan L/C included the cost of the cargo, insurance, and payment of the subfreights. Respondent INB was identified as the receiving (presenting) bank under the Shinhan L/C.

When INB initially attempted to draw down on the Shinhan L/C, it was unable to do so owing to discrepancies in the documents. POSCO refused to waive those discrepancies because it had learned of Cornish's arrest action served on INB. Subsequently, and after INB had interjected itself into the actual negotiations to obtain POSCO's agreement to waive those discrepancies, INB finally got the proceeds. It then applied all of them (including the subfreights) against old Ferromet debt under an assignment Ferromet had given to INB in exchange for financing.

INB successfully persuaded the Court of Appeals to change the fundamental nature of the lien on subfreights from an *in rem* action against the *res* itself, to an *in personam* claim against the payor POSCO. By so doing, it has been able able to keep the subfreights, despite the superior nature of Cornish's maritime lien rights vis-a-vis INB's land based security interest in the same fund (App. 11a). This Petition for Writ of Certiorari followed.[3]

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3. For a more detailed recitation of the facts and circumstances surrounding this voyage and the payment of the subfreights, the Court is respectfully referred to the Appellate and District Court opinions appended hereto.

REASONS FOR GRANTING THE WRIT

Introduction

The Second Circuit's decision in *Cornish* represents a significant change in the nature of the shipowner's lien on subfreights, and a fundamental deviation from the way that lien has been enforced. For the last 100 years, the lien has been treated as an *in rem* right charged against a specific *res*, and capable of enforcement (through an arrest) wherever that *res* could be located and identified.[4] In place of this traditional *in rem* remedy, the Second Circuit has now formulated an entirely new and limited cause of action, stating:

> Nevertheless, we believe that the *res* to which the owner's lien on subfreights attaches should not be conceived as specific funds, as plaintiffs' theory assumes, but rather as a debt.

(App. 11a).

By limiting the *res* solely to the underlying debt of the initial payor, the *Cornish* decision artificially limits the scope of the lien in two ways: first, it obligates the shipowner to identify, locate, and pursue the third party obligor (who often is unknown to the shipowner and outside United States judicial process); and, second, it limits the shipowner's potential targets by preventing seizure of the funds in the "payment pipeline" (*i.e.*, en route from the payor to payee but not yet received). By so doing, the decision also pulls most of the teeth out of the lien on subfreights, and tilts

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4. The only prerequisite to a successful exercise of the lien is that the shipowner do so before the subfreights had been received by the charterer in the ordinary course (*see* discussion at 10).

the commercial playing field in favor of the banks, which already have more than enough security devices to satisfy their needs.[5]

If the *Cornish* decision is allowed to stand, a shipowner will no longer be able to arrest subfreights prior to receipt by a charterer as they move through routine payment channels.

The decision is also in direct conflict with the Ninth Circuit's decision in *Beverly Hills Nat'l Bank & Trust Co. v. Compania de Navegacione Almirante S.A.*, 437 F.2d 301 (9th Cir.) (intervention or manipulation of a subfreight payment by a junior lienor would not act to defeat the shipowner's rights), *cert. denied*, 402 U.S. 996 (1971), and the First and Second Circuits' decisions in *American Steel Barge Co. v. Chesapeake & O. Coal Agency Co.*, 115 F. 669 (1st Cir. 1902), *reh'g denied*, 116 F. 857 (1st Cir. 1902); and *Oceanic Trading Corp. v. The Freights, Sub Freights and/or Demurrage of the Vessel Diana*, 423 F.2d 1 (2d Cir. 1970) (the focus of the lien is against the fund itself and subfreights maintain their identity as a *res* through and until the time they are received by the payee).

Additionally, the decision conflicts with the language of Rule C of the Supplemental Rules for Admiralty and Maritime Claims ("Rule C") itself, (which expressly provides an *in rem* remedy against freights that are or will be within the district during the pendency of the action).[6]

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5. Unlike a land based lendor, a shipowner does not have the luxury of time to examine the creditworthiness of its counterparts. Instead, and based upon the realities of worldwide shipping, the chartering of a vessel often takes place in a matter of hours. As such, the shipowner's lien on subfreight is one of the few means by which it can insure payment of the freight, and any decision which erodes the effectiveness of that lien will have negative ramifications on commerce.

6. By its very terms, Rule C(2) contemplates enforcement against the funds as they move into a district, as distinguished from enforcement essentialy against the payor as decided in *Cornish*.

Finally, the *Cornish* decision leaves practitioners with inconsistent authority as to where and under what circumstances the lien can be exercised, and will negatively impact worldwide commerce by severely limiting what has heretofore been the most effective means by which a shipowner can secure the payment of freight. Further review is therefore warranted in order to provide rationality, certainty, and uniformity to this vital area of maritime and commercial law.

I. Historical Overview of the Lien on Subfreights: The Enforcement of the Lien Through an Action *In Rem* Against a *Res*.

It has long been held that a shipowner can secure payments due under a contract of charter party by including, as an express provision in the contract, a lien on the "subfreights" earned in the operation of its vessel. *Marine Traders, Inc. v. Seasons Navigation Corp.*, 422 F.2d 804, 806 (2d Cir. 1970). The specific lien on subfreights has been described as an "ancient and standard charter provision", and has been included in the NYPE charter form since the early 19th century.[7] *See In re North Atlantic & Gulf S.S. Co.*, 204 F. Supp. 899, 904 (S.D.N.Y. 1962), *aff'd sub nom. Schilling v. A/S D/S Dannebrog*, 320 F.2d 628 (2d Cir. 1963); Healy, *Commentary on the 1981 Revision of the New York Produce Exchange Form Time Charter*, 13 J. Mar. L. & Com. 521 (1982). As such, this security device is the most widely used means by which shipowners in the time charter trade secure the payment of freight — the life blood of the industry.

Unlike a common law lien which is grounded on a personal obligation of the owner, the maritime lien has been described as a

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7. This charter is the most popular form in worldwide time charter trade. Trowbridge, *The History, Development and Characteristics of the Charter Concept*, 49 Tul. L. Rev. 743, 750 (1975).

special "property interest" in the vessel or other *res* (often called a *jus in re*) which permits the claimant to foreclose in an *in rem* action against that *res* as the "offending thing". T. Schoenbaum, *Admiralty & Maritime Law*, § 9-1 at 490-91 (2d ed. 1994); *see also Vandewater v. Mills*, 60 U.S. (19 How.) 82, 89 (1857); G. Gilmore & C. Black, *The Law of Admiralty*, §10-7, 20 (2d ed. 1975).

> It cannot be stressed too strongly that the intangible property against which the process issues is the offending *res*. . . . The intangible assets within the scope of this rule [Rule C] *are not the equivalent of a debt owed to a defendant who cannot be found within the district — they are the res itself against which the lien is to be executed.* 7A J. Moore, *Moore's Federal Practice*, ¶ C.13 at 683, 84 (2d ed. 1995) (Emphasis added).[8]

Traditionally, the lien can be enforced against the subfreight fund wherever it can be located, provided it is traceable and identifiable as a *res*. *Moore's Federal Practice*, ¶ C.13 at 684. *See also Bank of British N.A. v. Freights, etc., of the Hutton*, 137 F. 534, 536 (2d Cir. 1905). It is routinely enforced through *in rem* process under Rule C. *Saint John Marine v. United States*, 1994 AMC 2526 (S.D.N.Y. 1994); *DK Mfg. Co. v. The Freights and Sub-Freights of the S.S. Titan*, 1964 AMC 78 (S.D.N.Y. 1963).[9] In the alternative, a notification of the election to exercise the lien will also suffice. *Tarstar Shipping Co. v. Century Shipline, Ltd.*,

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8. As such, the *Cornish* decision runs broadside into Moore's analysis that the *res* is not the equivalent of a debt.

9. Specifically, Rule C(3) provides for a Warrant of Arrest in conjunction with an enforcement of a lien against property consisting in whole or part of freight, or the proceeds of such property.

451 F. Supp. 317 (S.D.N.Y. 1978), *aff'd*, 597 F.2d 837 (2d Cir. 1979).

II. The *Cornish* Decision, Which Limits Enforcement of the Lien Solely to an Action Against the Payor, Is in Conflict With Prior Circuit Court Decisions Which Allow an Arrest of the *Res* at Any Point in the Payment Chain Prior to Receipt by the Charterer.

By shifting the focus away from the *res* and directing it solely to the payor, the *Cornish* decision deviates starkly from the traditional framework and guidelines under which enforcement of this remedy has been allowed. Before reviewing how this deviation has created a split among the Circuits, however, it is important to digress for a moment to review how enforcement has been implemented.

As previously outlined, the principle means by which a shipowner can ensure the payment of freight is through enforcement of its lien on subfreights. Such a lien may be enforced by an action *in rem*, with the focus of that action directed against the "intangible property such as freight." T. Schoenbaum, *Admiralty & Maritime Law*, §9-1 at 206, 478 n. 1 (2d ed. 1994).[10]

> Thus, for [an *in rem*] action to succeed it is necessary that the intangible *res* be within the district — or that it will be during the pendency of the action — and that commingling or other handlings have not made it impossible to trace the *res* back to its

10. *See also* 2 T. Russel, *Benedict on Admiralty*, § 22 at 2-8, 10 (1995) ("The characteristic virtue of a proceeding *in rem* is that it operates directly upon the *res* as the titular respondent in the suit."); G. Gilmore & C. Black, *The Law of Admiralty*, at 35 (2d ed. 1975) ("The maritime law gives to the party aggrieved a right conceived of as a property interest in the tangible thing.").

original maritime source. 7A J. Moore, *Moore's Federal Practice*, ¶ C.13 at 684.[11]

Typically, and as seen in this case, subfreight litigations often involve a collision between the holder of a maritime lien and the holder of a land-based security interest. In these circumstances, the courts focus on the issue of whether the subfreight still maintained its character as a *res* at the time of the arrest, thereby enabling effective seizure under Rule C.

To resolve the issue, the courts have focused on the status of the "payment" in relation to the timing of the exercise of the shipowner's lien.[12] *See Marine Traders, Inc. v. Seasons Navigation Corp.*, 422 F.2d 804 (2d Cir. 1970) (A shipowner's lien on subfreight is discharged by a good faith payment to the charterer without notice of the shipowner's rights).[13] Traditionally, this inquiry has focused on whether the *res* had been received. It is on this point that the *Cornish* decision deviates from the First and the Seventh Circuits, as well as prior

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11. *See also* the *Hutton*, 137 F. at 534 (indiciating that a maritime lien attaches not only to the original subject of the lien, but also to whatever is substituted for it, and that the *lienholder may follow the proceeds wherever he can distinctly trace them*).

12. Payment necessarily contemplates the completion of the transaction — that is the receipt of the funds by the payee. *See generally* 60 Am. Jur. 2d, *Payment* § 1.

13. *See also J.S. Connor, Inc. v. Marine Transport Serv. Inc.*, 1981 AMC 359, 365 (D.Md. 1980) (good faith payment to charterer extinguishes the lien *on the freight)*; *Hall Corp. of Canada v. Cargo ex Steamer Mont Louis*, 62 F.2d 603, 605 (2d Cir. 1933) (shipowner's lien can be asserted *on the res* unless the charterer has been paid in good faith and prior to an exercise of the shipowner's lien right); *Actieselskabet Dampsk. Thorbjorn v. Harrison & Co.*, 260 F. 287, 290 (S.D.N.Y. 1918) (payment of freight before the exercise of the shipowner's lien will act to discharge the lien *on the res*) (emphasis added).

Second Circuit precedent in the *Diana*, 423 F.2d 1 (2d Cir. 1970) (which is addressed first).

The *Diana* highlights how radical a departure the *Cornish* decision is from mainstream jurisprudence. At issue in the *Diana* was the often recurring question of whether the subfreights had been paid to a charterer at the point in time when the shipowner exercised its lien (prior payment otherwise vitiating the ability to assert an *in rem* arrest against those funds). As is typical in many of these cases, the funds were in the hands of a neutral intermediary bank at the time of the arrest. In reversing the lower Court's decision, the Second Circuit stated:

> Even if at a trial the plaintiff Oceanic proves that, as disponent owner, it was entitled to a maritime lien on the subfreights or demurrage, it still must prove that payment had not been *made and received* by ARL [charterer]. This issue will call for the presentation of evidence to clarify when and how and with what understanding and instructions the consignee... sent the funds covering the demurrage due the Diana ... and whether at any time the fund was placed in the hands of ARL or credited or posted to its account in that bank. *If not, a serious question arises as to whether or not payment had actually been made.* . . . The leading case in which subfreights were attached by the owner before payment to the charterer was made is *United States v. Freights, etc., of the S.S. Mount Shasta*, 274 U.S. 466, 467 (1926).

Id. at 6 (emphasis added).

The decision in *Cornish*, limiting enforcement of the lien solely to a debt in the hands of the initial payor, is completely inconsistent with the *Diana* analysis. To highlight this inconsistency, under the new *Cornish* test, even if the subfreight in the *Diana* had been sitting in that intermediary bank, in a segregated cash account, and with a big neon sign over it stating **"the subfreights are here"**, the shipowner would not be able to arrest those funds. The court in the *Diana* got it right.

The *Cornish* decision is similarly at odds with the First Circuit's decision in *American Steel Barge Co. v. Chesapeake & O. Coal Agency Co.*, 115 F. 669 (1st Cir. 1902), *reh'g denied*, 116 F. 857 (1st Cir. 1902), often described as one of the premier decisions in this area of the law. In *American Steel Barge*, the First Circuit confirmed two fundamental elements of this lien, which have now been implicitly rejected in the *Cornish* decision. First, the Circuit Court in *American Steel Barge* confirmed that the procedural mechanism for enforcement of the lien is an action against the subfreight itself (not just a debt), and second, such process can be served on anyone "with the possession thereof" (not just the initial obligor). The court goes on to note that if the party with possession of the *res* fails to honor the lien by depositing the freight into the registry of the Court, that party can be subjected to process. *American Steel Barge*, 115 F. at 674.

There is absolutely no discussion in *American Steel Barge* of a limitation on the enforcement of the lien solely to a debt in the hands of the original obligor (the new *Cornish* test). The important distinction is that while the remedy of an *in personam* action has *always* existed against an original obligor who violates a timely exercise of the lien, the *Cornish* decision makes that remedy the exclusive enforcement mechanism, thus conflicting with the First Circuit.

The *Cornish* decision is also in conflict with the Seventh

Circuit's analysis in *Union Industrielle et Maritime v. Nimpex Int'l.*, 459 F.2d 926 (7th Cir. 1972). In that case, the court's discussion regarding the status of the *res* (which was actually sub-subfreight) indicates that *Cornish's* artificial limitations placed on the scope of the enforcement of the lien would not be adopted.

In considering whether a shipowner was able to exercise a lien over certain sub-subfreights, the *Nimpex* court examined the status of the party who was in possession of that *res* at the time of the arrest.[14] Implicit in its analysis was the need to determine whether the payment had been received thereby changing the character of the *res.* As such, *Nimpex* confirms that in the Seventh Circuit, the lien is not limited solely to a debt in the hands of the payor.

The *Cornish* decision can not be squared with one of the premier English decisions on point either. *Tagart, Beaton & Co. v. James Fisher & Sons,* 1 K.B. 391 (C.A. 1903). In this early English decision from which much of the current subfreight lien law is based, the court recognized that subfreights exist as a *res* capable of being arrested through and until the point where they are received by the payee:

> (T)he right over the freight must be exercised at a time when there is freight to be paid as such, and that when the freight has once been paid the lien upon it is gone. The moment that the freight has been paid over by the consignees to persons who are entitled to receive it, the shipowner's right *to stop it on its way* ceases to exist. *Id.* at 394 (emphasis added).

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14. *See* discussion at 459 F.2d at 930 regarding status of Hoesch Export.

Implicit in *Tagart* is the recognition that the fund exists as an independent jural entity (*i.e., a res*) capable of being arrested while in the payment pipeline until such time as received. There is nothing in *Tagart* to suggest that a shipowner's ability to exercise its lien right against that *res* should be circumscribed so as to prevent a seizure while the funds are en route. Indeed, *Tagart* suggests just the opposite with its reference to stopping the subfreights "on its way." Certainly, *Tagart* does not support the *Cornish* rationale that such right of seizure should be pushed back in time — beginning and ending with the obligor.

One of the most irreconcilable aspects of the *Cornish* decision is its reliance on the Supreme Court's decision in the *United States v. Freights, etc. of the S.S. Mount Shasta,* 274 U.S. 466 (1927). In *Cornish,* the Second Circuit used the *Mount Shasta* as the springboard upon which to base its conclusion that the lien could only be enforced against the debt in the hands of the payor. Remarkably, the *Mount Shasta* was also relied upon by the Second Circuit in the *Diana* case, in which a wholly different result was reached (arrest of a *res* en route and while in the hands of a neutral, intermediary bank not prohibited).[15]

Contrary to the restrictive interpretation currently attached by the Second Circuit in *Cornish* to the *Mount Shasta,* that case actually served to promote rather than restrict the enforceability of a shipowner's lien on subfreights. Admittedly, the *Mount Shasta* addressed the status of a debt owing by the payor, however, that discussion related to an effort by the defendant payor to divest the Court of the jurisdiction by denying that there was any subfreight owing. It was in this context that the Supreme Court determined that it had the jurisdiction to examine whether there was a *res* upon which to support *in rem* jurisdiction.

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15. Certainly the *Mount Shasta* cannot form the underpinning for two decisions which are in direct conflict.

The *Mount Shasta* decision, however, in no way limited the exercise of the lien on subfreights *solely* to the circumstances when the debt was still held by the payor. As is evident, the *Cornish* decision has created confusion warranting intervention by this Court.

III. The Court of Appeals' Decision Is Also in Conflict With the Ninth Circuit's Decision in *Beverly Hills*: Under *Cornish*, Intervention by a Junior Lienor Is Now Ignored.

There is yet another split, this one between the Ninth and Second Circuits on the question of whether intervention or manipulation on the part of the competing secured party — like INB — will nevertheless result in the shipowner losing its lien on subfreights on the basis that mere "payment", under any circumstances, will kill the lien.

In the Ninth Circuit, under the *Beverly Hills Nat'l Bank & Trust Co. v. Compania de Navegacione Almirante S.A.*, 437 F.2d 301 (9th Cir.), *cert. denied*, 402 U.S. 996 (1971) decision, it is clear that such conduct or intervention on the part of a junior competing creditor in garnering the subfreights will simply not be tolerated. In its examination of whether the shipowner's entitlement to the subfreights would be primed by the bank's rights, the Ninth Circuit reviewed in detail the bank's conduct in procuring those subfreights, indicating that an obligation would be imposed upon the bank to maintain those funds in the form of a constructive trust if any manipulation was found. *Beverly Hills*, 437 F.2d at 307.

The Ninth Circuit's discussion of the need to evaluate the conduct of an assignee recipient like INB dovetails with other precedent under which the loss of this lien has been reviewed. The requirements of "good faith" and payment in the "ordinary course" have been read into the subfreight test for decades,

indicating that the shipowner's lien will be lost only if the transfer is completed *absent* any interference or manipulation.[16]

The *Cornish* decision reads out of the subfreight test the requirement that the payment transaction occur in the ordinary course and in good faith before a shipowner's lien will be lost against that *res.*[17] The bank clearly enjoyed POSCO's misconception on this point, and indeed INB even fooled its own customer Ferromet who repeatedly demanded that INB live up to its bargain to satisfy Cornish upon transfer of the Shinhan L/C proceeds. [18] In fact, under *Cornish,* such conduct is ignored all together.

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16. *See Marine Traders*, 422 F.2d 804 (discussing requirement of "good faith" payments); *Hall Corp.*, 62 F.2d at 605 (discussing good faith element in the transfer of subfreights); *Larsen v. 150 Bales of Sisal Grass*, 147 F. 783 (S.D. Ala. 1906) (requiring transfer to have been made in the "ordinary course"); and Gilmore & Black, *The Law of Admiralty* at 233 (again referring to the need that the payment be made in ordinary course).

17. It is noteworthy that virtually all of the factors which would have prompted a duty to hold the funds under the Ninth Circuit's discussion in *Beverly Hills* are present in this case. There is evidence of fraud on the part of INB, to the extent that it used a freight "pre-paid" bill of lading to draw down on the Shinhan L/C, while fully aware the freight had not been paid to Cornish. There was a confidential relationship between INB and Ferromet, a relationship not disclosed to POSCO during the negotiations resulting in POSCO's agreement to waive the documentary discrepancies.

18. Further, POSCO was clearly operating on the assumption that a portion of the Shinhan L/C proceeds representing subfreights would be used to satisfy Cornish, as Ferromet had repeatedly indicated to POSCO that the subfreight payment was needed for that very purpose. Finally, INB was unjustly enriched, since its own security agreement precluded assertion of claims against what was described as "permitted liens", which included liens of a materialman like Cornish. For a review of the criteria evaluated by the Ninth Circuit, *see Beverly Hills*, 437 F. 2d at 307.

The new rule announced by the Second Circuit in *Cornish* is completely at odds with the Ninth Circuit's decision in *Beverly Hills*. In the Second Circuit, all that counts is that the assignee bank get the *res* out of the hands of the payor — by hook or by crook. As such, conduct similar to that of INB's will be encouraged. Since the obligation of good faith is imposed on any party who asserts a maritime lien, *see The Kate*, 164 U.S. 458, 466-68 (1896), this Court should impose the same obligation on a junior lienor like INB who seeks to destroy a maritime lien to its own benefit.

CONCLUSION

This case cries out for a Writ for Certiorari. Like a collision at sea in broad daylight — inconsistent treatment of a maritime lien between the Circuits is not supposed to happen. It promotes uncertainty in a business community that, by its very nature, requires uniformity. Moreover, clarification on this point will discourage unwarranted intervention by junior lienors who seek to attack a shipowner's superior lien on subfreight. The shipowning community needs this Court to throw it a line, as was extended 75 years ago in the *Mount Shasta*, when a similar effort was mounted to undermine this important lien. The petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DATED APRIL 20, 1995

CORNISH SHIPPING LTD.,

Plaintiff-Appellant,

Pohang Iron & Steel Co., Ltd.,

Intervenor-Plaintiff-Appellant,

v.

INTERNATIONAL NEDERLANDEN BANK N.V., f/k/a NMB Postbank Groep, N.V.,

Garnishee-Defendant-Appellee.

* * *

No. 1126, Docket 94-7786.

United States Court of Appeals,
Second Circuit.

Argued Jan. 18, 1995.

Decided April 20, 1995.

Peter J. Gutowki, New York City (Michael Fernandez, Freehill, Hogan & Mahar; and Bryan Cave, and Steven R. Haffner, on the brief), for plaintiff-appellant and intervenor-plaintiff-appellant.

Appendix A

John M. Toriello, New York City (James H. Hohenstein, Haight, Gardner, Poor & Havens; and Peter E. Calamari, and Anthony L. Paccione, Hertzog, Calamari & Gleason, on the brief), for garnishee-defendant-appellee.

Before: NEWMAN, Chief Judge, MINER and CABRANES, Circuit Judges.

JON O. NEWMAN, Chief Judge.

This appeal in an admiralty case presents a novel question concerning the scope of a shipowner's maritime lien on subfreights. At issue is whether the lien attaches to funds that were paid to a charterer after the owner gave notice of the lien to the payor. The question arises on an appeal by plaintiff Cornish Shipping Ltd. ("Cornish") and plaintiff-intervenor Pohang Iron & Steel Co., Ltd. ("POSCO") from the April 20, 1994, judgment of the District Court for the Southern District of New York (Kimba M. Wood, Judge), which granted the summary judgment motion of garnishee-defendant International Nederlanden Bank, N.V. ("INB") in an action to recover funds paid to INB in its capacity as agent and assignee of a charterer of a ship owned by Cornish. Because we conclude that a shipowner's lien on subfreights does not attach to funds that have been paid to the charterer or its agent, we affirm.

Background

Parties and contractual provisions. This case arose out of an ill-starred voyage of the cargo vessel M/V *Filoktitis* from United States Gulf ports to Korea. In the Fall of 1991, defendant Ferromet Resources, Inc. ("Ferromet") contracted to sell and deliver American steel scrap to plaintiff-intervenor POSCO, C.I.F. Korea. POSCO was to pay Ferromet for the scrap, its

transport, and insurance under a letter of credit issued on POSCO's behalf by Shinhan Bank ("Shinhan"). Ferromet could draw down the Shinhan letter of credit upon presentation of specified documents, including bills of lading and original invoices for the scrap. The sales invoice submitted by Ferromet to POSCO indicated that approximately $1.6 million of the total price for the steel scrap was attributable to the cost of transport ("freight value").

On its end, Ferromet received financing for this transaction from defendant-garnishee INB, with which it had an established credit relationship. INB advanced $3.3 million to cover the acquisition of the steel scrap and the cost of charter hire. As part of this financing transaction, Ferromet assigned to INB all moneys to become due under it October 10 contract with POSCO and further agreed that INB could apply moneys that it received from POSCO to the repayment of any of Ferromet's outstanding obligations to INB. A financing statement covering this assignment was filed in Florida at the end of 1991. This security arrangement supplemented security interests that INB had previously acquired in Ferromet's property, including its current and future accounts receivable.

To transport the shipment of steel scrap to Korea, Ferromet time-chartered the cargo vessel M/V *Filoktitis* from its owner, plaintiff Cornish. Under the terms of the charter party, Ferromet agreed to pay freight to Cornish at the rate of $13,750 per day, and Cornish reserved a lien on all subfreight earned by the Filoktitis for amounts due under the charter.[1] In addition to the steel scrap,

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1. "Freight" is the hire paid by the charterer to the owner for the use of the latter's vessel. *See* 2 Thomas J. Schoenbaum, *Admiralty and Maritime Law* § 1-11, at 194 (2d ed. 1994). "Subfreights" are amounts that third-party payors — whether subcharterers, shippers or consignees — contract to pay directly to the charterer for the hire of the ship or the transport of goods. *See* 2 *id.* § 11-17, at 207 n. 25.

Ferromet planned to use the *Filoktitis* to transport a cargo of stainless steel, which it was selling to POSCO under a separate contract and separate financing arrangements.

Voyage of the Filoktitis. In January 1992, the cargoes of stainless steel and steel scrap were loaded onto the *Filoktitis* at United States Gulf ports, and bills of lading were issued to Ferromet. By the end of the month, Ferromet had delivered to INB the documents required to draw down the Shinhan letter of credit in payment for the scrap shipment. Acting as Ferromet's collecting bank INB notified Shinhan on February 3 of certain discrepancies in these documents, which would have to be waived by POSCO before the letter of credit could be drawn down.

These discussions between INB and Shinhan were immediately overtaken by events triggered by the impending insolvency of Ferromet. On February 3, the same day that INB began discussions with Shinhan, Cornish notified POSCO that Ferromet had defaulted on its payment of freight and that Cornish was exercising its lien on any subfreights due from POSCO to Ferromet. Cornish's notice of lien also informed POSCO that the *Filoktitis* had been detained in Panama because Ferromet had not paid Canal dues and because another creditor of Ferromet had attached the bunkers of the *Filoktitis* to secure payment of hire for another ship, the M/V *Grigoroussa*. The next day, Cornish filed in the District Court a complaint against Ferromet, initiating the present action. Pursuant to Rule C of the Supplemental Rules for Certain Admiralty and Maritime Claims, which governs *in rem* actions for the enforcement of maritime liens, the District Court issued warrants for the arrest of the subfreight of the *Filoktitis*. These warrants were served on five banks in New York, including INB, on February 4, and again on February 13 and February 21.

Appendix A

As a result of the ensuing negotiations between all parties to the escalating controversy, INB eventually agreed to place $250,000 in escrow, as a loan to Ferromet, to cover the dispute with the owners of the *Grigoroussa*, and POSCO agreed to waive the discrepancies in the documentation required by the Shinhan letter of credit.[2] Thus, on February 20, 1992, INB, acting as Ferromet's collecting bank, was able to draw down the letter of credit, including amounts that Ferromet had billed as "[sub]freight" charges; INB immediately credited the proceeds to the outstanding principal of its loan to Ferromet. INB then withdrew from further negotiations regarding the freight installments that Ferromet had failed to pay to Cornish.

Cornish reacted to these events the next day by obtaining an *ex parte* order from a Panamanian court authorizing arrest of the cargo aboard the *Filoktitis*. The ship was then detained in Panama for an additional two and one-half months while Cornish and POSCO tried to work out a compromise. During this interval, an involuntary bankruptcy petition was filed against Ferromet. Finally, on May 11,1992, Cornish and POCO entered into an agreement settling their disputes relating to the voyage. Pursuant to this settlement, POSCO agreed to pay Cornish $650,000 and to share other expenses, and Cornish agreed to transport the cargo of the *Filoktitis* to Korea. The cargo was finally delivered to POSCO on June 30.

District Court proceedings. In the District Court, Cornish argued that approximately $1.6 million of the proceeds that INB

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2. The parties dispute whether INB also represented to POSCO that it would use the proceeds from the letter of credit to resolve Cornish's claim for the freight payments defaulted on by Ferromet. Under our holding in this case, this factual dispute is not material to, whether Cornish's lien attaches to the funds that were paid to INB.

had collected on the Shinhan letter of credit represented subfreights subject to Cornish's maritime lien on subfreights, and that INB violated the Court's Rule C arrest warrants when it credited those funds to its own account. POSCO, with Cornish's consent, intervened as plaintiff on a subrogation theory, claiming a stake in any recovery from INB to the extent of the payments POSCO had made to Cornish under their May 11 settlement agreement. In response to the plaintiffs, INB argued that once the proceeds of the letter of credit were transferred to it in its capacity as collecting agent for Ferromet, those proceeds ceased to be subeights to which Cornish's lien attached. On cross-motions for summary judgment, the District Court upheld INB's legal theory and, finding that no material facts were in dispute, entered summary judgment dismissing Cornish's and POSCO's claims against INB. *See Cornish Shipping Ltd. v. Ferromet Resources, Inc,* 1995 A.M.C. 235, 1994 WL 171717 (S.D.N.Y.1994) (mem. op. and order). Pursuant to Fed.R.Civ P. 54(b), the District Court ordered entry of a final judgment on these claims.[3]

Discussion

The primary issue on this appeal is whether a shipowner's lien on subfreights attaches to funds that a consignee remits to a charterer after the consignee has received notice that the

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3. A claim by Cornish against Ferromet for breach of the charter party remains before the District Court pending its resolution in, Ferromet's bankruptcy proceedings in Texas. POSCO has also filed a proof of claim against Ferromet in the bankruptcy court, including a claim for freight costs it paid under the May 11 settlement agreement with Cornish. In addition, POSCO had previously initiated a suit against INB and Ferromet in New York Supreme Court, alleging a cause of action, among others, for common law fraud in connection with the February 20 agreement with INB, in which POSCO wahred the discrepancies in the documentation required to draw down the Shinhan letter of credit.

shipowner is exercising its lien. Although this precise issue has not previously been resolved, prior cases and important policy considerations favor the view that a shipowner's lien on subfreights represents a contingent right to collect a debt directly from a consignee, rather than a right to specific funds that the consignee intends to use or has used to satisfy that debt. In accordance with this view, we conclude that the shipowner's lien does not give it a right to trace specific funds that the consignee has paid to a charterer.

Most aspects of the law governing a shipowner's maritime lien on subfreights are well established. To secure payments of freight due from a charterer of its ship, a shipowner may create, by express provision in the charter party, a lien on the subfreights earned by the vessel. *Marine Traders Inc. v. Seasons Navigation Corp.*, 422 F.2d 804, 806 (2d Cir.1970). Subfreights are amounts that third-party payors—whether subcharterers, shippers, or consignees (generically "consignees")—contract to pay to the charterer for the use of the ship or the transport of goods.[4] If the charterer defaults on its payment of freight or its other obligations under the charter party, the shipowner may exercise its lien on the subfreights by giving notice to the consignee. Before such notice is given, however, the lien is essentially inchoate. Indeed, the lien is altogether extinguished if the consignee pays the subfreights to the charterer or its agent in good faith prior to receiving notice of the lien. *See Tarstar Shipping Co. v. Century Shipline, Ltd,* 597 F.2d 837, 839-40 (2d Cir. 1979); *Union Industrielle et Maritime v. Nimpex International Ltd.*, 459 F.2d 926, 929 (7th Cir.1972); *Beverly Hills National Bank & Trust Co. v. Compania de*

4. For the owner's lien on subfreights to be effective against shippers or consignees, we have stated that the terms of the charter party must also be restated in or incorporated by reference into the bill of lading. *See Oceanic Trading Corp. v. Freights of the Vessel Diana,* 423 F.2d 1, 5 (2d Cir.1970).

Navegacione Almirante S.A., 437 F.2d 301, 304 (9th Cir.), *cert. denied*, 402 US. 996, 91 S.Ct. 2173, 29 L.Ed.2d 161 (1971); *Marine Traders*, 422 F.2d at 806; *Hall Corp. of Canada v. Cargo ex Steamer Mont. Louis*, 62 F.2d 603, 605 (2d Cir.1933); *MCT Shipping Corp. v. Sabet*, 497 F.Supp. 1078, 1084-85 (S.D.N.Y. 1980); *In re North Atlantic & Gulf Steamship Co.*, 204 F.Supp. 899, 904 (S.D.N.Y. 1962), *aff'd sub nom. Schilling v. A/S D/S Dannebrog*, 320 F.2d 628 (2d Cir.1963).

Cornish satisfied the established requirements for asserting its lien on the subfreights of the *Filoktitis*. The lien was created under the terms of the charter party and incorporated into the bill of lading, and Cornish (the shipowner) gave notice to POSCO (the consignee) that it was exercising its lien before POSCO took the final steps necessary to authorize payment of "freight" charges to INB, the agent of Ferromet (the charterer). Thus, the established rule that the lien is extinguished if the consignee makes payment to the charterer *prior to* receiving notice of the lien does not resolve the issue in this case. When a consignee pays ostensible "subfreights" to the charterer *after* receiving notice of the lien, as occurred here, such payment does not discharge the *consignee's* liability for the sub-freights to the owner. *See Tarstar*, 97 F.2d at 839-40; *North Atlantic & Gulf*, 204 F.Supp. at 904. Thus, precisely because Cornish asserted its lien by giving notice to POSCO before POSCO paid subfreights to Ferromet, Cornish has a cause of action *against* Posco that would not otherwise be available to it.

Cornish and POSCO join, however, in seeking an additional remedy *against INB*. They argue that if a shipowner gives timely notice of its lien prior to payment of the subfreights by the consignee; the lien attaches to the subfreight funds as a *res*, and the lien then follows those funds into the hands of any recipient

who has notice of the lien, including the charterer or its agent.[5] According to this view, Cornish's primary remedy is against INB, because INB received the subfreight funds after the lien had attached and after INB itself had received notice of the lien via service of Cornish's Rule C arrest warrant.[6] In response, INB argues that the owner's lien on subfreights confers no right to follow the subfreight funds after they have been paid to the charterer or its agent, because payment destroys the funds' character as an independent to which the lien can attach. In spite of each side's vigorous insistence that its theory has been clearly established by prior cases, we have found no authority that directly confronts the issue of whether the additional remedy claimed by Cornish and POSCO is available when subfreights are paid after the consignee has received notice.[7] To resolve this

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5. It is not entirely clear that Cornish is making a traditional lienor's argument that the lien attached to the funds as they moved from POSCO to INB. At oral argument, counsel suggested that the funds might not have been subject to a lien as they moved to INB, but that, in some metaphysical sense, they encountered the barrier of the lien plus the Rule C arrest warrant just prior to coming into INB's possession.

6. In the event that the recipient subsequently commingles the liened fund with other monies, Cornish and Posco also contend that the shipowner can proceet against the recipient *in personam* for violation of the lien.

7. The District Court relied on Judge Sand's opinion in *MCT Shipping, supra*, as authority for the proposition that payment of subfreights to the charterer or its agent extinguishes the shipowner' lien, even if such payment occurs after the shipowner notifies the payor that it is exercising the lien. However, a careful review of the facts reported in *MCT Shipping* indicates that in that case the shipper probably paid the subfreights to the charterer *before* the owner notified the shipper of its lien. Among other indications, the court and parties in *MCT Shipping* appeared to agree that the payment discharged the *shipper's* liability to the owner as well as the charterer, *see* 497 F.Supp. at 1085, which would not be true if the payment were paid after the owner had given notice of its lien.

dispute, it is necessary to take a broader view of the conceptual underpinnings and policy implications of the parties' rival theories.

On the surface, Cornish's and POSCO's position has substantial plausibility. In American admiralty law, "the existence of a maritime lien is synoymous with the availability of a libel *in rem*." Grant Gilmore & Charles L. Black Jr., *The Law of Admiralty* 622 (2d ed. 1975); *see also* 7A James W. Moore et al., *Moore's Federal Practice* ¶ C.02, at 609 (2d ed. 1993); Supp.R.Adm. & Mar.Claims C(1)(a) (action *in rem* may be brought to enforce any maritime lien). It is not unreasonable to assume that in the case of the owner's lien on subfreights, the pertinent *res* is the specific funds that the consignee pays or intends to pay to the charterer for tranport. *See* 7A Moore et al, *supra*, ¶ C.13, at 683 ("freights—which are *moneys paid* for the transportation of cargo . . . — may be liened" (emphasis added)). Moreover, we have stated, in an older case involving a different type of lien on freights, that once a lien attaches to such funds, the lien follows the proceeds through all of their traceable transmutations:

> The lien created by a maritime pledge of freights follows the freights through all their transmutations, and wherever they can be found. It is familiar doctrine of the admiralty courts that a maritime lien attaches not only to the original subject of the lien, but also to whatever is substituted for it and that the lienholder may follow the proceeds wherever he can distinctly trace them. "Wherever there is a maritime lien upon property, it adheres to the proceeds of that property, into whose

> hands soever they may go, and these proceeds may be attached in the admiralty."

Bank of British North America v. Freights of the Hutton, 137 F. 534, 536 (2d Cir.1905) (quoting Benedict, *Admiralty Practice* § 290 (3d ed.)); *see also In re Bauer Steamship Corp.*, 167 F.Supp. 909, 911 (S.D.N.Y.1957). Once timely notice has been given, permitting the lienor to follow the subfreight funds into the hands of the charterer also has the apparent practical advantage that the lienor cannot be deprived of his lien merely because the consignee erroneously pays the funds to the charterer. Moreover, if the lien does attach to these funds, its maritime character would give the shipowner priority over rival claimants with land-based security interest, even interests created earlier in time, *See In re Topgallant Lines, Inc.*, 154 B.R. 368, 376 (S.D.Ga.1993), *aff'd sub nom, McAllister Towing v. Ambassador*, 20 F.3d 1175 (11th Cir.1994); *Taiwan International Line Ltd. v. Matthew Ship Chartering Ltd.*, 546 F.Supp. 826, 829 (S.D.N.Y.1982); Gilmore & Black, *supra*, at 734.

Nevertheless, we believe that the *res* to which the owner's lien on subfreights attaches should not be conceived as specific funds, as plaintiffs' theory assumes, but rather as a debt. Linguistically, the term "subfreights" appears to be used to refer both to the consignee's debt for freight costs and to the actual monies used or intended to be used to pay that debt. It is important to distinguish between these two meanings in the present context. If the owner's lien attaches to subfreights as a debt, the exercise of that lien should vest the owner with the rights that the charterer would otherwise have under the contract of affreightment to proceed against that debt. The owner then becomes, in effect, the assignee or subrogee of the charterer's rights; as such, however, the owner does not accede to any additional rights beyond those

that the charterer formerly had. On this theory, once the owner gives timely notice of its lien to the consignee, the consignee's obligation to pay the debt for subfreights runs exclusively to the owner, and any subsequent payment to the charterer does not extinguish that obligation. But because maritime law does not give the charterer an interest in any specific funds in the consignee's accounts,[8] the owner should not receive such an interest when it is subrogated to the rights of the charterer.

Several considerations favor the conclusion that the shipowner's lien attaches to the debt for subfreights, rather than to specific subfreight funds. First, in *United States v. Freights of S.S. Mount Shasta,* 274 U.S. 466, 470, 47 S.Ct. 666, 670-71, 71 L.Ed. 1156 (1927), the Supreme Court held that admiralty's *in rem* jurisdiction over subfreights does not require the existence of specific funds, but extends to a debt for subfreights, even a debt that is disputed and unliquidated. In reaching this result, the Court noted:

> By the general logic of the law a debt may be treated as a *res* as easily as a ship. It is true that it is not tangible, but it is *a right of the creditor's, capable of being attached* and appropriated by the law to the creditor's duties.

Id. (emphasis added). If, as *Mount Shasta* implies, the *res* that is "capable of being attached" is "a right of the creditor's," ie., of the charterer then exercise of that power of attachment should

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8. The chartererr has a possessory lien on cargo to secure the consignee's payment of subfreights, *see North Atlantic Gulf,* 204 F.Supp. at 904; 2 Schoenbaum, *supra,* at 207, but not a lien on any funds in the consignee's accounts.

work an assignment of that intangible right to the shipowner. In accordance with this view, several cases have expressly characterized a shipowner with a valid lien on subfreights as standing "in the eyes of the admiralty . . . with all the rights of an assignee under a deed of assignment," *American Steel Barge Co. v. Chesapeake & Ohio Coal Agency Co.*, 115 F. 669, 673 (1st Cir.1902), so that "[a]t the proper time, and under the proper circumstances, a libelant holding a lien on subfreight becomes subrogated to all the remedies of the charterer," *id.* at 674; *accord Luckenbach Overseas Corp. v. Subfreights of the S.S. Audrey J. Luckenbach*, 232 F.Supp. 572, 575, 577 (S.D.N.Y.1963); *Larsen v. 150 Bales of Sisal Grass*, 147 F. 783, 785 (S.D Ala.1906); *see also MCT Shipping*, 497 F.Supp. at 1085 ("Once the freight is paid, the owner, insofar as he stands in the charterer's shoes, is entitled to nothing." (emphasis added)). The shipowner's lien has also been said to be "derivative" of the charterer's remedies against the consignee. 2 Schoenbaum, *supra*, at 207; *see also North Atlantic & Gulf Steamship*, 204 F.Supp. at 904; *Bauer Steamship Corp.*, 167 F.Supp. at 910. Since the charterer's rights do not include a lien on specific subfreight funds in the consignee's account, the shipowner's attachment of those rights should not carry with it a lien on any specific funds.

The conclusion that the shipowner's lien on subfreights attaches to the charterer's legal rights to collect a debt for subfreights from the consignee, rather than to any specific funds that the consignee has designated for payment of that debt, receives support from the traditional rule that the lien is extinguished if the consignee pays the charterer in good faith before receiving notice of the lien. If it were true that the lien gave the owner an interest in the subfreights as funds, it would be logical for the owner to be able to execute the lien against those funds, or any identifiable portion of them, even if the consignee

had paid them to the charterer before receiving notice of the lien. Under those circumstances, payment prior to notice should, at most, discharge the consignee's personal liability, rather than extinguish the owner's lien altogether. On the other hand, if the lien attaches to the subfreight only as a debt, it is easy to see why payment prior to notice completely extinguishes the lien: in that case, there is no longer any debt to attach. *Cf. Tartar,* 597 F.2d at 840 (where subfreights are paid to agent of charterer prior to notice, they "los[e] their character as an independent *res* to which the owner's lien could attach").

Thus, to the extent that plaintiffs' argument depends on the theory that Cornish's lien attached directly to the funds that POSCO had designated as subfreights and then followed those funds into INB's accounts, their argument fails. However, the funds that POSCO remitted to INB might still be conceived as the *proceeds* of the debt to which Cornish's lien attached. Under the above quoted language of *The Hutton* 137 F. at 636, "a maritime lien attaches not only to the original subject of the lien, but also to whatever is substituted for it, and . . . the lienholder may follow the proceeds wherever he can distinctly trace them."[9] In our view,

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9. Although *The Hutton* also concerned a lien on freights, it was significantly different from the lien at issue here: in order to secure advances from his bank, the charterer in *The Hutton* had granted the bank a lien on the freights that he collected from specific voyages financed by the bank. *See* 137 F. at 535-36. Because by its terms the bank's lien attached directly to the funds after they were paid to the charterer, rather than to the charterer's chose in action against the payor, *The Hutton* did not present the question whether the funds received by the charterer represented the proceeds of a debt that had been assigned to another party. In addition, In *The Hutton* the funds that the lienholder succeeded in tracing back to the subfreights were still in the charterer's own accounts. Thus, *The Hutton* was *not* a case in which the proceeds of attached property had to be traced into the hands of a third party, and its sweeping language concerning the lienholder's right to trace such proceeds went far beyond its facts. We note that despite their putative "indelibility," maritime liens

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however, this fund does not represent "proceeds" of the debt that Cornish is entitled to follow. Once POSCO received notice of the lien, and thus of the "assignment" to Cornish of Ferromet's rights as subfreight creditor, POSCO cold extinguish the debt only through payment to Cornish or its agents, not to Ferromet or its agents. Since POS-CO's remittance to INB did not represent payment of the attached debt for subfreights, the monies remitted were not the debt's proceeds, and they therefore may not be traced by Cornish. Of course, the logical corollary is that neither the debt for subfreights—the *res* to which the lien attached—nor the lien itself could be extinguished by POSCO's transfer of the funds to INB. *See North Atlantic & Gulf*, 204 F.Supp. at 904 (timely notice of lien "bars the shipper from discharging his liability for the subfreights by payment to the charterer"). That transfer was, at bottom, irrelevant to Cornish's right to execute the lien by proceeding against POSCO for payment of the debt. *See Tarstar*, 597 F.2d at 839-40 (payment to charterer after notice of lien does not extinguish owner's right to proceed against subcharterer).

A comparison with the provisions of the Uniform Commercial Code governing security interests in accounts receivable helps to illuminate the limitations of the shipowner's lien on subfreights.[10] Like the shipowner's lien, a U.C.C. security

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(Cont'd)

are often defeated by a defense of laches if the attached property or its proceeds has passed into the hands of a purchaser without notice of the lien. *See* Gilmore & Black, *supra*, at 7665.

10. Maritime liens and land-based liens, such as article 9 security interests, have been characterized as "two unlike things . . . called by the same name." Gilmore & Black, *supra*, at 589; *see also In re Pacific Caribbean Shipping (U.S.A.), Inc.*, 789 F.2d 1406, 1407 (9th Cir. 1986). It would therefore be inapt to construe the scope of maritime lines on analogy with land liens. Nonetheless, because

(Cont'd)

interest in accounts receivable gives the secured party a priority interest in debts that an account debtor owes to the secured parts primary debtor. Article 9 of the U.C.C. gives the secured party two distinct remedies for enforcing this security interest, only one of which is available to the holder of a maritime lien on subfreights. First, upon default by the primary debtor, the secured party is entitled to notify account debtors that they are to make payments directly to it, rather than to the primary debtor. *See* U.C.C. § 9-502(1); *Community Bank v. Newmark & Lewis, Inc.*, 534 F.Supp. 456, 460 (E.D.N.Y.1982). In effect, notice to the account debtor under section 9-502(1) subrogates the secured party to the rights of the primary debtor—the remedy that is available to enforce a shipowner's lien. In addition, however, a party with a security interest in accounts receivable also has a continuously perfected interest in the identifiable cash proceeds of those accounts, *i.e.*, in the payments remitted by the account debtor to the primary debtor. See U.C.C. §§ 9-306(3)(b), (4), -502(1). But this interest in proceeds is entirely independent of the secured party's right of subrogation. Even if the secured party has not instructed an account debtor to pay him directly, under section 9-306 his security interest ordinarily attaches to proceeds of the debt that are paid to the primary debtor. A shipowner, in contrast, has no analogous interest in subfreight payments that are made to a charterer before the owner gives notice that it is exercising its lien. The shipowner's lien gives it the right to seek payment of subfreights from the consignee or other payor, but not the analytically distinct right to take control of payments that the consignee makes to the charterer or its agent.

(Cont'd)

subfreights are akin to accounts receivable, *see Topgallant Lines*, 154 B.R. at 374, article 9's treatment of security interests in accounts may provide useful tools for analyzing subfreight liens.

This narrow construction of the shipowner's lien on subfreights also adheres to longstanding judicial policy:

> Because the maritime lien is a secret lien arising by operation of law, "[i]t may operate to the prejudice of prior mortgagees or of purchasers without notice. It is therefore *stricti juris* and will not be extended by construction, analogy or inference."

Itel Containers International Corp. v. Atlanttrafik Express Service Ltd., 982 F.2d 765, 768 (2d Cir.1992) (quoting *Piedmont & Georges Creek Coal Co. v. Seaboard Fisheries Co.*, 254 U.S. 1,12, 41 S.Ct. 1, 4, 65 L.Ed. 97 (1920)). The facts of this case well attest to the importance of this policy. INB possessed security interests in Ferromet's current and after-acquired receivables long before Cornish and Ferromet entered into the charter party that created Cornish's lien on the subfreights. Although INB had notice of Cornish's lien in February 1992, when it received the proceeds of the Shinhan letter of credit, the priority accorded a maritime lien would still work to the prejudice of rights the bank had acquired years before it had such notice. The fate of the *Filoktitis* in Panama also illustrates how the multiplication of these secret liens can "hamper[ ] instead of advance ease and freedom of commerce," *The Saturnus*, 250 F. 407, 414 (2d Cir.), *cert. denied*, 247 U.S. 521, 38 S.Ct. 583, 62 L.Ed. 1247 (1918).

The countervailing policy arguments advanced by Cornish and POSCO are less persuasive. They maintain that limitations on a shipowner's means for enforcing its lien will harm maritime commerce by undermining one of the few devices available to secure the payment of freight. But a shipowner's remedies are not

unduly restricted by our holding. In addition to an *in personam* claim against the charterer for freights due under the charter party, a shipowner who has given timely notice of its lien obtains the right to proceed directly against the consignee for subfreights due. Once it has attached, this latter right cannot be defeated by the consignee's erroneous payment to the charterer, because that payment is irrelevant to the consignee's liability to the owner. Although the additional remedy of being able to attach funds that were erroneously paid to the charterer would be of great value to Cornish under the facts of this case, the prospective value of this additional remedy to shipowners in general is so uncertain that its presence is unlikely to affect their willingness to enter into charters. This is especially so because the security offered by the lien on subfreights is by its nature tenuous, subject to complete defeasance by payment to the charterer prior to notice.

We are also not persuaded by Cornish's and POSCO's contention that the rule we adopt will encourage charterers and their agents to deal in bad faith, as plaintiffs suggest INB did when it negotiated with POSCO for the waiver necessary to draw down the Shinhan letter of credit. Insofar as Cornish is concerned, INB's conduct simply had no effect on Cornish's rights to enforce its lien against POSCO. As for POSCO, sufficient state law remedies are available if, as plaintiffs intimidate, INB in fact fraudulently induced it to waive the discrepancies or breached a contract to forward a portion of the proceeds to Cornish in satisfaction of the latter's lien. Expanding the scope of the shipowner's lien is not necessary to fraud. In the event that a consignee is in doubt about which party has the right to receive payment for freight costs, it can deposit an appropriate sum in escrow pending judicial resolution of the question. *See Taiwan International Line*, 546 F.Supp. at 829.[11]

Appendix A

Conclusion

The judgment of the District Court, granting INB's motion for summary judgment, is affirmed.

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11. Our resolution of the main issue on this appeal renters moot plaintiffs' argument that prior service on INB of a Rule C arrest warrant for the subfreights prevented, as a matter of law, INB from validly receiving the subfreight fund, and that therefore the transfer of funds from POSCO could not have extinguished Cornish's lien because it did not constitute legal payment of the subfreights to the charterer or its agent. Under our holding above, Cornish's lien did not attach to the specific funds transferred by POSCO to INB; at the same time, this transfer was ineffective to extinguish Cornish's lien on POSCO's debt for subfreights. We note, in addition, that plaintiffs' argument incorrectly assumes that a Rule C arrest warrant is effective against property that comes into the possession of a garnishee after service of the warrant. *See Reibor International Ltd. v. Cargo Carriers (KACZ-CO.) Ltd.*, 759 F.2d 262 (2d Cir. 1985) (holding that Rule B attachment does not extend to after-acquired property); *see also Union Planters National Bank v. World Energy Systems Associates*; 816 F.2d 1092; 1098 (6th Cir. 1987). Although *Reibor* concerned an order of attachment under Rule B of the Supplemental Rules, the policy considerations that motivated the Court in *Reibor* apply with equal force to Rule C arrests. *Cf. United States v. All Monies of Banco Cafetero International*, 608 F.Supp. 1394, 1403-04 (S.D.N.Y. 1985) (applying *Reibor* rule to Rule C arrest in forfeiture action) *aff'd*, 797 F.2d 1154 (2d Cir. 1986).

APPENDIX B — MEMORANDUM OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK DATED APRIL 5, 1994.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

92 Civ. 0857 (KMW)

CORNISH SHIPPING LTD.,

Plaintiff,

-against-

FERROMET RESOURCES, INC.

Defendant,

INTERNATIONAL NEDERLANDEN BANK N.V., f/k/a/ NMB POSTBANK GROEP, N.V.,

Garnishee

POHANG IRON & STEEL CO., LTD.,

Intervening Plaintiff,

-against-

INTERNATIONAL NEDERLANDEN BANK N.V., f/k/a/ NMB POSTBANK GROEP, N.V.,

Garnishee-Defendant

Appendix B

MEMORANDUM OPINION AND ORDER

Wood, D.J.

Plaintiff Cornish Shipping Ltd ("Cornish") and intervening plaintiff Pohang Iron & Steel Co., Ltd. ("Posco") move for summary judgment on their entitlement to Posco's subfreights payment of approximately $1.6 million, which was received and retained by garnishee-defendant International Nederlanden Bank N.V. ("INB").[1] INB cross-moves for summary judgment, seeking dismissal of the claims asserted against it by Cornish and Posco. For the reasons set forth below, the court denies Cornish's and Posco's motion and grants INB's motion.

BACKGROUND

Cornish was the owner of the ocean going cargo vessel M\V Filokitis (the "Vessel"). On December 6, 1991, Cornish chartered the Vessel to Ferromet Resources, Inc. ("Ferromet") for the purpose of transporting a cargo of steel scrap products (the "Steel Shipment") from U.S. ports to Korea for delivery to Posco, the purchaser of the cargo. INB, as Ferromet's banker, agreed to finance the transaction. INB advanced $3.3 million to Ferromet to cover the cost of the charter hire and acquisition of the Steel Shipment. As part of the transaction, Ferromet assigned to INB the proceeds of the Steel Shipment to be paid by Posco, including the purchase price of the steel, insurance, and the cost of shipping the cargo (i.e., the subfreights). The payment was to be made under a letter of credit dated December 3, 1991 (the "Steel L/C"), which was issued by Posco's banker, Shinhan Bank.

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1. The term "subfreights" generally refers to the payment of ocean freight by the cargo receiver or shipper, in this case Posco, to a vessel charterer or its agent. *See* Wilford, Coghlin & Healy, *Time Charters* (30 ed. 1978), at 224.

Appendix B

In January 1992, the Steel Shipment was loaded on the Vessel. Under the agreement between Ferromet and Posco, the Steel L/C became payable upon loading the cargo and presentation of appropriate commercial documents to Shinhan Bank. By February 3, 1992, INB began discussions with Shinhan Bank to arrange a draw-down of the Steel L/C. INB notified Shinhan of certain discrepancies in the documents required for draw-down of the Steel L/C, and Posco withheld payment pending resolution of those discrepancies.

In late January 1992, shortly after the Vessel departed from Tampa, Ferromet became delinquent in its charter payments to Cornish. In response, Cornish exercised a maritime lien on the subfreights by serving notice of the lien on Posco. Cornish also commenced Rule C arrest proceedings in this court against, among others, INB. The Rule C arrest warrant included notification that Cornish had exercised its lien on the subfreights. INB received the Rule C arrest and the verified complaint to this action on February 4, 1993.

Meanwhile, the Vessel had arrived at the Panama Canal in late January, and Silverose Marine Ltd. ("Silverose"), a party unrelated to the present action, had attached the fuel bunkers of the Vessel as security for a separate claim that Silverose had against Ferromet. Subsequently, Ferromet, Cornish, Silverose, Posco and INB entered into negotiations to resolve both the Silverose and Cornish claims. Pursuant to these negotiations, INB agreed to post $250,000 in escrow to cover the dispute with Silverose, and Posco agreed to disregard the discrepancies in the documents presented by INB to draw down the Steel L/C. Thus, on February 20, more than two weeks after INB received notice of Cornish's lien on the subfreights, INB presented the documents to Shinhan Bank and drew down the proceeds of the

Steel L/C, including the subfreights against which Cornish had exercised its lien. Pursuant to its agreement with Ferromet, INB applied the Steel L/C proceeds to the outstanding principal of the loan used to finance the Steel Shipment. INB subsequently withdrew from the continuing negotiations between Ferromet, Cornish and Posco regarding the charter hire that Ferromet had still failed to pay to Cornish.

On February 21, 1992, Cornish obtained an *ex parte* order from the Panamanian court authorizing arrest of the cargo aboard the Vessel. As a result, the Vessel remained in Panama for over two months while the remaining parties attempted to resolve their dispute. On March 17, Ferromet entered bankruptcy. On May 11, Posco and Cornish reached an agreement under which Posco agreed to pay Cornish $650,000 and to share other expenses, in exchange for which Cornish agreed to transport the Steel Shipment to Korea. Under this agreement, Posco was compelled to pay Cornish an amount reflecting a portion of the subfreights that Posco had already paid to INB under the Steel L/C. Subsequently, the Vessel departed from Panama and the cargo was delivered to Posco on June 30.

By this motion, Cornish seeks to enforce its Rule C arrest warrant against INB by requesting that the court order INB to turn over approximately $1.6 million of the $2.9 million that INB collected under the Steel L/C. Cornish asserts that the $1.6 million constitutes subfreights to which it is entitled by virtue of its maritime lien on the subfreights and the Rule C arrest warrant. Cornish also seeks damages beyond the amount of the subfreights on the grounds that INB violated the Rule C arrest warrant.

Posco, as intervening plaintiff, joins Cornish in this motion and asserts that it is entitled to recovery against INB for the

$650,000 that Posco paid to Cornish to gain release of the Steel Shipment in Panama. Posco's theory of recovery is that having paid part of Ferromet's debt to Cornish, it is entitled to damages as a subrogee of Cornish.

INB opposes the motion of Cornish and Posco, and cross-moves for summary judgment. INB asserts that it is entitled to retain all of the proceeds of the Steel L/C and has not violated any order of this court. INB contends that once the Steel L/C proceeds were transferred by Shinhan Bank to INB, those proceeds ceased to be subfreights of the Vessel and thus are no longer a *res* to which a maritime lien can attach. Cornish and Posco dispute this contention.

DISCUSSION

Summary judgment is appropriate when "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c); *Citizens Bank of Clearwater v. Hunt,* 927 F.2d 707, 710 (2d Cir. 1991). Here, Cornish and Posco move for summary judgment and INB cross-moves for summary judgment on the issue of entitlement to $1.6 million of the Steel L/C proceeds. No party to this motion contends that there is a genuine issue of material fact that would preclude summary judgment on this question. Comparison of Local Rule 3(g) statements and counterstatements confirms that no genuine issue of material fact exists. Moreover, the parties' competing claims of entitlement to $1.6 million of the Steel L/C proceeds depend upon whether a maritime lien on the subfreights of a vessel is effective as against a charterer and its agent in the undisputed circumstances of this case. This is manifestly a question of law. Summary judgment is therefore appropriate.

Appendix B

As noted above, the question of law at issue is whether a vessel owner's maritime lien on the vessel's subfreights is effective as against a charterer and its agent. Resolution of the question requires consideration of the principles governing the exercise and termination of the maritime lien on subfreights, and application of these principles to the complex and unusual (although substantially undisputed) facts of this case.

A vessel owner may create, by express provision in a charter party, the right to exercise a lien on the subfreights earned by the vessel, i.e., payments due the charterer from the shipper for shipment of the cargo. *See Marine Traders. Inc. v. Seasons Navigation Corp.*, 422 F.2d 804, 806 (2d Cir. 1970). Here, Cornish, the vessel owner, reserved the right to exercise a lien against the subfreights to be paid by Posco, the cargo shipper, to Ferromet, the charterer.

A shipowner exercises its maritime lien on subfreights by giving notice of the lien to the cargo shipper, prior to the shipper's payment of the subfreights. *See In re North Atlantic and Gulf S.S. Co.*, 204 F. Supp. 899, 904 (S.D.N.Y. 1962), *aff'd*, 320 F.2d 628 (2d Cir. 1963). Once paid to the charterer, however, subfreights lose "their character as an independent *res* to which that the owner's lien [can] attach." *Tarstar Shipping Co. v. Century Shipline Ltd.*, 597 F.2d 837, 839-40 (2d Cir. 1979). Thus, if the shipper makes good faith payment of the subfreights to the charterer before the shipper has notice of the shipowner's lien, any such lien is extinguished. *Marine Traders Inc. v. Seasons Navigation Corp.*, 422 F.2d 804, 806 (2d Cir. 1970); *Hall Corp. of Canada v. Cargo Ex Steamer Mont Louis. etc.*, 62 F.2d 603, 605 (2d Cir. 1933). However, once a shipper receives notice of a shipowner's lien on unpaid subfreights, the shipper may not discharge his liability to the shipowner by paying the charterer. *In*

re North Atlantic and Gulf S.S. Co., 204 F. Supp. at 904. Rather, a shipper who disregards notice of a shipowner's lien against unpaid subfreights and pays the subfreights to the charterer or his agent, remains liable to the shipowner in the amount of the subfreights. *See e.g., Tarstar Shipping Co.*, 597 F.2d at 840.

In this case, the cargo shipper, Posco, received notice of Cornish's lien on the subfreights at a time when it still held the subfreights. Notwithstanding its receipt of the notice of lien, Posco subsequently paid the subfreights to the charterer's bank, INB. Thus, under established maritime law principles, Posco did not discharge its liability to Cornish when it paid the subfreights to INB. *See In re North Atlantic*, 204 F. Supp. at 904.

Posco's subsequent actions are consistent with an awareness that its liability to Cornish was not discharged by its payment of the subfreights to INB. Posco paid $650,000 to Cornish as part of a settlement under which Cornish agreed to release Posco's cargo from arrest in Panama. Posco characterizes this payment as "an amount reflecting a portion of the [sub]freight proceeds Posco had already paid" to INB. Posco Br. at 4. As a result of its settlement agreement with Cornish, Posco made payments to INB and Cornish totalling 140 percent of the value of the subfreights. If Posco had not reached its settlement with Cornish, it could have been liable for 200 percent of the value of the subfreights; that is, it would have had to pay Cornish, as well as INB, the full value of the subfreights. *See Tarstar Shipping*, 597 F.2d at 840 (shipper that pays subfreights to the charterer notwithstanding prior receipt of vessel owner's notice of lien required to pay the subfreights twice).

Against this background, Cornish and Posco are now joined as plaintiffs in this action against INB, in which Cornish seeks

recovery of Posco's $1.6 million payment to INB, and Posco claims subrogation to the extent of its $650,000 payment to Cornish. Cornish and Posco put forth, in essence, a theory of joint and several liability for shipper and charterer where, as here, both parties were served with a notice of lien prior to payment of the subfreights. The court concludes that the claim advanced by Cornish and Posco is inconsistent with established maritime law principles and, as such, must be rejected.

Cornish and Posco seek to expand the scope of the maritime lien on subfreights by urging that the lien survives payment of the subfreights to the charterer (or its agent) if the charterer was previously notified of the lien. In support of this proposition, Cornish and Posco point to the lack of clear authority to support the contrary proposition. Cornish and Posco Br. in Response to INB Sur-Reply, at 3.

In considering Cornish's and Posco's argument, the court begins by noting the principles governing the judicial construction of maritime liens. It is well established that maritime liens are strictly construed. *See generally Benedict on Admiralty,* § 24 (1993 ed.) (citing cases). Over fifty years ago the Supreme Court stated:

> The maritime lien is a secret one. It may operate to the prejudice of prior mortgagees or of purchasers without notice. It is therefore *stricti juris* and will not be extended by construction, analogy or inference.

Piedmont & Georges Creek Coal Co. v. Seaboard Fisheries Co., 254 U.S. 1, 12 (1920). Applying this rule of strict construction, the Second Circuit rejected a claim for extension of a maritime

lien, emphasizing that such extension could significantly disrupt maritime commerce:

> The ancient ... lien of the sea is not maintained ... for the convenience or assurance of the parties, but for the encouragement of commerce and shipping .... Anything more than this multiplies secret liens and hampers instead of advances ease and freedom of commerce. Merchant and mariner alike subject their property to the municipal law of every country into which their venture comes, but a maritime lien is as near an approach to jus gentium as can be found in private jurisprudence and any extension thereof not internationally well founded is to be opposed as jealously as is a denial of its accepted extent.

The Saturnus, 250 F. 407, 414 (2d Cir.), *cert. denied,* 247 U.S. 521 (1918).

Applying these principles more recently, Judge Sand rejected the claim that a maritime lien may attach to subfreights that have already been paid to a charterer's agent. *See MCT Shipping Corp. v. Sabet,* 497 F. Supp. 1078 (S.D.N.Y. 1980). Judge Sand cogently articulated the policy concerns underlying strict construction of the maritime lien on subfreights:

> [W]e conclude that plaintiff's maritime lien on subfreights persists only for as long as the subfreights remain unpaid by the shippers involved .... Once the freight is paid, the

> owner, insofar as he stands in the Charterer's shoes, is entitled to nothing. He retains, of course, his essentially contractual claim against the Charterer, but once that claim is resolved, his standing among the Charterers' other creditors should be adjudicated on its merits without regard to the priority and security afforded by a maritime lien. Extending the 'reach' of the owner's lien to funds already in the hands of a Charterer or its agent would have a more far reaching and less predictable impact on the Charterer's other creditors. The owner's priority interest would survive, and in each case, the Court would be required to identify those funds held by the Charterers or one or more of its agents which are traceable as subfreights of a particular vessel on a particular voyage .... [W]e believe that a clear line must be drawn between paid and unpaid freights because of the limited purpose of a maritime lien, as well as the potential difficulty of identification in other cases.

MCT Shipping, 497 F. Supp. at 1085.

The present case differs from *MCT Shipping* only in that notice of the lien in that case was received by the charterer's agent *after* he received the subfreights payment. By contrast, in this case, INB had notice of Cornish's lien prior to receipt of the subfreights payment. Cornish and Posco assert that the timing of the notice distinguishes *MCT Shipping* from this case. The court disagrees. The policy concerns articulated by Judge Sand and the

general rule of strict construction of maritime liens apply with equal force to the present case. Moreover, there is ample authority discussed below to support the conclusion that notice of a lien to a charterer or its agent, even where given prior to their receipt of the subfreights payment, does not prevent such payment from dissolving the lien.

Cornish and Posco contend that Cornish's Rule C arrest warrant gave INB notice of Cornish's lien on the subfreights, thereby preserving the lien notwithstanding transfer of the subfreights from shipper's agent Shinhan Bank to charterer's agent INB, which transfer would normally discharge such a lien. *See MCT Shipping*, 497 F. Supp. at 1085. As noted above, plaintiffs point to an alleged lack of authority to support the opposite proposition, i.e., that a subfreights payment to a charterer, or his agent, discharges a lien, even where the charterer had notice of the lien prior to receipt of the payment.[2] *See* Cornish

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2. Cornish and Posco also rely heavily on the decision in *DK Mfg. Co. v. The Freights and Sub-Freights of the S.S. Titan*, 1964 A.M.C. 78 (S.D.N.Y. 1963), which they contend provides unambiguous support for their claim. In *D.K. Mfg.*, a bank was ordered to deposit in the registry of the court an amount equal to certain subfreights to which it may have come into possession as agent and assignee of the charterer. However, the court expressly reserved decision concerning entitlement to the funds, stating that the claims of all parties were a question of fact to be determined at trial. 1964 A.M.C. at 80. Even if *D.K. Mfg.* can be understood as providing some support for Cornish's claim, that position would conflict with the plain language of *Tarstar Shipping Co.*, 597 F.2d at 840 (had the funds been in the hands of the charterer's agent, the funds "would have lost their character as an independent res to which an owner's lien could attach"), and the Judge Sand's well-reasoned opinion in *MCT Shipping Corp*, 497 F. Supp. at 1085; *c.f. In re Bauer Steamship Corp.*, 167 F. Supp. 909, 910-11 (S.D.N.Y. 1957) (subfreights already paid to bankrupt charterer subject to shipowner's lien, where bankruptcy referee had entered order that payment of subfreights would be made without prejudice to shipowner's lien).

and Posco Br. in Response to INB Sur-Reply, at 3. However, the decisions of this Circuit strongly suggest that the only relevant notice of a shipowner's lien is notice to a cargo shipper or to another paying party, not to the recipient of the subfreights payment.

> If the cargo is delivered and the shipper pays the sub-freights to the charterer in good faith, the shipowner's lien falls .... However, the shipowner may, at any time prior to payment of the sub-freights by the shipper, assert his lien by giving *notice to the shipper* of its existence .... *Such notice* bars the *shipper* from discharging his liability from the sub-freights by payment to the charterer.

In re North Atlantic and Gulf S.S. Co., 204 F. Supp. 899, 904 (S.D.N.Y. 1962), *aff'd*, 320 F.2d 628 (2d Cir. 1963) (citations omitted) (emphasis added). *See also* Wilford, Coghlin & Kimball, *Time Charters* (3 ed. 1989) at 409 ("The lien may be exercised on sub-freights . . . only if the sub-charterer or shipper has notice of the shipowner's lien and has not yet paid the sub-freights to the charterer"). Thus, plaintiffs' argument that prior notice to the charterer has the effect of giving the shipowner a lien on subfreights as against the charterer does not avail. In this case, the only party upon whom Cornish's notice of lien had any legal effect was Posco, the cargo shipper.[3] The court cannot sanction plaintiffs' effort to extend the maritime lien against subfreights by manipulating the notice of lien requirement to apply to charterers as well as shippers.

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3. Cornish exercised its maritime lien on the subfreights then held by Posco through the service on Posco's agent of a notice of lien dated February 3, 1992. Posco does not dispute that it was properly notified of the lien.

Similarly, the court must reject plaintiffs arguments regarding the rule that a lien against subfreights is discharged upon "good faith" payment of the subfreights. Plaintiffs argue that INB's conduct lacked good faith, such that any payment of subfreights to INB did not have the effect of discharging Cornish's lien. Cornish's Reply Br., at 23-5. Leaving aside whether INB acted in good faith (as the court must on this summary judgment motion), the court finds INB's good faith irrelevant to whether payment discharged the lien. As with the notice requirement discussed above, the good faith rule applies only to the shipper or other paying party, in this case Posco. *See Marine Traders Inc.*, 422 F.2d at 806 ("a shipowner's lien on subfreights is discharged by good faith payments by the shipper to the charterer"). While Posco's payment of the subfreights under the Steel L/C was perhaps ill advised, no one has suggested that it was done in bad faith.

In summary, the effect of Cornish's notice of lien ran exclusively to Posco. Notwithstanding notice of the lien, Posco paid the subfreights to INB, agent and assignee of the charterer Ferromet. Upon transfer to charterer's agent INB, the funds ceased to be subfreights, thereby losing the character of a res against which a maritime lien could attach. *See Tarstar Shipping Co.*, 597 F.2d at 840. Thus, Cornish's claim of a maritime lien on the Steel L/C funds now held by INB must fail.

Cornish and Posco assert in the alternative that INB, as Ferromet's assignee, was not entitled to the subfreights because "the exercise of Cornish's lien nullified INB's personal interest in the subfreights." Cornish Reply Br., at 27. The movants fail to acknowledge that INB was acting as Ferromet's agent as well as its assignee, *see* Cornish Exh. 11, and was entitled to collect the Steel L/C funds in its capacity as Ferromet's agent. *See Tarstar Shipping Co.*, 597 F.2d at 840 (had the funds been in the hands of

the "*agent* of the charterer, we do not doubt that the freights would already have been paid and would have lost their character as an independent *res* to which the owner's lien could attach") (emphasis added). Moreover, even if INB is viewed as acting solely in its capacity as Ferromet's assignee, INB is still entitled to collect the Steel L/C proceeds. *See Beverly Hills Nat'l Bank & Trust Co. v. Compania de Navegacione Almirante S.A.*, 437 F.2d 301 (9th Cir.), *cert. den.*, 402 U.S. 996 (1971) (where bank received subfreights as assignee of charterer, vessel owner's lien on these funds were extinguished); *see also J.S. Connor Inc. v. Marine Transport Services Inc.*, 1981 A.M.C. 359 (D. Md. 1980), *aff'd mem.*, 673 F.2d 1312 (4th Cir. 1982). Cornish and Posco attempt to distinguish those decisions by noting that they concerned subfreights that were received by the assignee before the exercise of the vessel owner's lien. Although the movants' factual distinction is correct, the court rejects the inference that a different result would have occurred if the funds had been received by the assignees after the exercise of the vessel owner's lien. The court's determination on this motion — that a lien against subfreights does not survive payment of the subfreights, even where the recipient of the subfreights payment has prior notice of the lien — applies to a charterer's agent or assignee as well as to the charterer.[4]

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4. In holding that the $1.6 million Steel L/C proceeds held by INB are not "subfreights" to which Cornish's lien can attach, the court also concludes that INB did not violate Cornish's Rule C warrant of arrest. Accordingly, the court denies that branch of Cornish's motion seeking damages beyond the amount of the "subfreights" on the grounds that INB violated the Rule C warrant of arrest. Similarly, the court denies Posco's separate motion for a determination that it is entitled to subrogation.

Appendix B

CONCLUSION

For the reasons stated above, the court denies Cornish's and Posco's motion for summary judgment and grants INB's cross-motion for summary judgment. The clerk of the court is directed to enter judgment for defendant-garnishee International Nederlanden Bank N.V..

SO ORDERED.

Dated: New York, New York
April 5, 1994

s/ Kimba M. Wood
Kimba M. Wood
United States District Judge

Copies of this opinion have been mailed to counsel for the respective parties.

(2) No. 95-130

Supreme Court, U.S.
FILED
AUG 22 1995
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

CORNISH SHIPPING LTD.,

Petitioner,

—v.—

INTERNATIONAL NEDERLANDEN BANK N.V.,
f/k/a NMB POSTBANK GROEP, N.V.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION

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QUESTION PRESENTED FOR REVIEW

1. Did the Second Circuit Court of Appeals and District Court for the Southern District of New York correctly deny a shipowner's attempt to extend a maritime lien on subfreights to reach funds that had been paid to a charterer's agent?

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.1 of the Supreme Court Rules, respondent Internationale Nederlanden Bank N.V., formerly known as NMB Postbank Groep, N.V. ("INB") has a publicly traded parent corporation: ING Group, Amsterdam, The Netherlands.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

No. 95-130

CORNISH SHIPPING LTD.,

Petitioner,

—v.—

INTERNATIONAL NEDERLANDEN BANK N.V.,
f/k/a NMB POSTBANK GROEP, N.V.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION

Statement of the Case

A. Introduction

This case presents neither the conflicts the Petition alleges nor any other issues worthy of this Court's review. In a well-reasoned opinion by Chief Judge Jon O. Newman, the U.S. Court of Appeals for the Second Circuit affirmed the District Court's decision concluding that "a shipowner's lien on sub-freights does not attach to funds that have been paid to the charterer or its agent . . ." (App. 2a). Accordingly, the Second Circuit properly determined that Cornish was not entitled to assert a maritime lien on a portion of the proceeds of a

letter of credit paid to the charter's lender, INB, which was indisputably the charterer's agent for purposes of collection as well as the assignee of the letter of credit proceeds. Contrary to the arguments raised by Petitioner, Cornish Shipping Ltd. ("Cornish" or "Petitioner") this result is neither extraordinary nor is it in contravention of other circuit court decisions.

B. Background

The present dispute arises out of a New York Produce Exchange Form charter by Ferromet Resources, Inc. ("Ferromet") of the M/V FILOKTITIS from its owner, Cornish. Ferromet intended to use the vessel to transport two shipments of steel scrap to Korea pursuant to a contract between Ferromet, as seller, and Pohang Iron & Steel Co. Ltd. ("POSCO"), as purchaser. In order to pay Ferromet for the steel scrap, as well as insurance and the transportation costs of the steel scrap, POSCO opened an irrevocable letter of credit at Shinhan Bank ("Shinhan L/C").

For a period of several years prior to the transaction at issue, Ferromet had a credit relationship with INB. In the context of this relationship, Ferromet received financing from INB as well as other banks. INB and Ferromet had entered into a loan agreement for one of the scrap steel cargoes which ultimately was loaded on the FILOKTITIS. INB did not negotiate the terms of Ferromet's sale to POSCO nor its charter of the vessel; it simply provided financing to Ferromet for this transaction. As part of its security, INB received an assignment of the proceeds of the POSCO sale and accordingly made appropriate U.C.C. security filings. INB advanced more than $3.38 million to Ferromet for the transaction.

In early January 1992, the scrap steel destined for Korea was loaded on the FILOKTITIS. On January 30, 1992, INB received the documents from Ferromet necessary to draw down on the Shinhan L/C. In accordance with standard banking practice, INB reviewed the documents and dutifully

notified Shinhan Bank of five minor discrepancies appearing in the documents. On February 3, 1992, Cornish sent a notice of lien on subfreight to POSCO and Shinhan Bank. Because of the minor documentary discrepancies identified by INB, POSCO was able to prevent the immediate drawdown of the letter of credit.

At or about the same time, an unrelated Ferromet creditor attached the bunkers (fuel oil) aboard the FILOKTITIS while the vessel was at the Panama Canal. The bunkers ostensibly were Ferromet's property and subject to attachment by its creditor.

Given its various financial problems, Ferromet approached INB for assistance in resolving the situation. Thus, INB entered negotiations with Ferromet, Cornish, POSCO and the unrelated creditor in order to lift the bunker attachment in Panama. As a result of the negotiations, INB advanced an additional $250,000 to Ferromet to fund an escrow covering the disputed claim of the unrelated creditor. In addition, INB agreed to fund a further loan to Ferromet in the amount of $52,000 for Panama Canal fees and other charges.

In exchange for INB's agreement to provide these further advances to Ferromet which would resolve the dispute with the unrelated creditor, POSCO agreed to waive the documentary discrepancies under the Shinhan L/C. POSCO sent a letter to INB, which reflects the terms of the agreement between INB and POSCO. There is no mention in the letter of any promise by INB to pay Cornish's hire claim against Ferromet for the simple reason that no such promise ever was made by INB. This letter was a part of the record below. Despite Cornish's sweeping assertions to the contrary, which were made both before the District and Circuit Courts, no competent evidence ever was submitted to any court that INB acted wrongfully.[1]

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[1] Further, as noted by the appellate court below, POSCO had subsequently initiated a suit against INB and Ferromet in New York Supreme

In accordance with the POSCO/INB agreement, INB escrowed $250,000 and advanced the Panama Canal fees. The unrelated creditor's attachment of the vessel's bunkers was lifted. On the same day, Shinhan Bank confirmed POSCO's waiver of the discrepancies under the Shinhan L/C and the payment to INB was made by wire transfer through international banking channels. INB then applied the payment ($2,995,426.01) to reduce the $3.3 million loan made to Ferromet to finance the scrap steel transaction. However, even after application of the L/C payment, Ferromet still owed INB an additional $16 million from this and other transactions.

Not content with the assertion of its lien against POSCO, Cornish then obtained an *ex parte* Order from the Panamanian Court and arrested the cargo onboard the vessel, despite Cornish's prior issuance of bills of lading for the cargo which were marked "freight pre-paid". The vessel then remained in Panama for 82 days while Cornish and POSCO litigated whether Cornish's cargo arrest was valid. Ultimately, Cornish and POSCO reached an agreement whereby POSCO paid Cornish $650,000 to obtain the release of the cargo. On May 15, 1992, the vessel left Panama and proceeded to Korea where it discharged the cargo.

After a period of discovery, Cornish, the intervening plaintiff, POSCO, and INB presented cross-motions for summary judgment before the District Court.[2] After the District Court

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Court, alleging a cause of action, among others, for common-law fraud in connection with the POSCO/INB agreement (App. 6a n.3). After the Second Circuit's decision, POSCO and INB entered into a stipulation of dismissal of the state court action. Consequently, the state court action has now been dismissed. Of course, POSCO, the supposed aggrieved party, has not joined in Cornish's certiorari petition.

[2] Even though Cornish made repeated attempts to make an issue of INB's supposed misconduct in this matter, it commenced yet another action against INB in the Southern District of New York after entry of the District Court's judgment and while the present matter was *sub judice* before the Second Circuit. That action improperly seeks to spin off common law claims arising from the same transaction as in this Petition.

found in INB's favor, Cornish and POSCO appealed to the Appellate Court below. In affirming the finding of the District Court, the Circuit Court carefully considered Cornish's and POSCO's arguments but rejected their positions.

Reasons for Denying the Petition

In the decision below, the Second Circuit reviewed the nature of the *res* that was the subject of the lien on subfreights. The court determined that that lien reaches the debt for subfreights, but does not reach any particular funds in the consignee's account, or more pertinently, in the charterer's own accounts. Petitioner misconstrues the holding of the Second Circuit and overlooks the court's rationale. Chief Judge Newman summarized the court's holding:

> Although this precise issue has not previously been resolved, prior cases and important policy considerations favor the view that a shipowner's lien on subfreights represents a contingent right to collect a debt directly from a consignee, rather than a right to specific funds that the consignee intends to use or has used to satisfy that debt. In accordance with this view, we conclude that the shipowner's lien does not give it a right to trace specific funds that the consignee has paid to a charterer.

(App. 7a).

Chief Judge Newman explained that the exercise of the lien "should vest the owner with the rights that the charterer would otherwise have under the contract of affreightment to proceed against that debt." (App. 11a).

This holding and rationale is perfectly in accord with precedent and the public policy underlying the strict construction of maritime liens. Contrary to Petitioner's assertion, there is

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Cornish's new action against INB currently is before the District Court and INB intends to defend that matter vigorously.

no conflict among the circuits, nor is the decision a radical revision of the maritime lien on subfreights. Indeed, Cornish's overstatement that the Second Circuit decision "pulls most of the teeth out of the lien on the subfreights" (Petition at 5) is belied by Cornish's ability in this case to force POSCO to settle by paying an additional $650,000 in freight to Cornish after it already had paid more than one million dollars for the freight to Ferromet.

In seeking the review of the decision of the Second Circuit, Cornish chooses to blink at its ability to enforce the lien on subfreights in the traditional manner by asserting it against the payor of the debt. By defining further the nature of subfreight that is affected by the lien, the Second Circuit reaches a conclusion that is in accord with prior case law. In sum, a shipowner such as Cornish remains able to seek redress against the payor, but as before, simply cannot attempt to trace and recover funds from the charterer or its agent.

POINT I

A MARITIME LIEN IS NOT MAINTAINED FOR THE ASSURANCE OF THE PARTIES INVOLVED. IT IS A SECRET LIEN WHICH IS INTENDED TO PROMOTE COMMERCE AND SHIPPING. IT IS STRICTLY CONSTRUED AND NOT SUBJECT TO EXPANSION SO AS TO AVOID CREATION OF OBSTRUCTIONS TO INTERNATIONAL COMMERCE

As recognized by both courts below (App. 17a, 27-28a), it is a well-established principle that maritime liens are construed strictly and disfavored in the law. In *Piedmont & Georges Creek Coal Co. v. Seaboard Fisheries Co.*, 254 U.S. 1, 12 (1920), this Court stated:

> The maritime lien is a secret one. It may operate to the prejudice of prior mortgagees or of purchasers without

> notice. It is therefore *stricti juris* and will not be extended by construction, analogy or inference.

Any attempt to extend the reach of a maritime lien should be summarily rejected, where such an extension would interfere with the settled course of maritime affairs, *see, e.g., Tramp Oil and Marine, Ltd. v. M/V MERMAID I*, 805 F.2d 42, 46 (1st Cir. 1986) or disrupt the normal course of international commerce. *Cf. A/S Dampskibsselskabet Torm v. Beaumont Oil Ltd.*, 927 F.2d 713, 721 (2d Cir.), *cert. denied*, 502 U.S. 862 (1991) (financing bank not liable for freight charges due to disturbing effect on banking and commerce).

As expressed more than 70 years ago:

> The ancient . . . lien of the sea *is not maintained . . . for the convenience or assurance of the parties, but for the encouragement of commerce and shipping . . . .* Anything more than this multiplies secret liens and hampers instead of advances ease and freedom of commerce. Merchant and mariner alike subject their property to the municipal law of every country into which their venture comes, but a maritime lien is as near an approach to jus gentium as can be found in private jurisprudence and any extension thereof not internationally well founded is to be opposed as jealously as is a denial of its accepted extent.

The SATURNUS, 250 F. 407, 414 (2d Cir.), *cert. denied*, 247 U.S. 521 (1918) (emphasis added); *see also Itel Containers Int'l Corp. v. Atlanttrafik Express Serv. Ltd.*, 982 F.2d 765 (2d Cir. 1992).

Before the District and Circuit Courts, Cornish (and POSCO) sought to expand the scope of a maritime lien on subfreight beyond any previous decision. The District Court properly rejected the attempt. So too, the appellate court below recognized that allowing the multiplication of these secret liens can lead to the disruption, not advancement, of

maritime commerce as exemplified by the fact that Cornish was prosecuting its supposed lien claims both in the District Court and the Panamanian Court. (App. 17a).

POINT II

THE DECISION OF THE COURT BELOW WAS NOT AN "EXTRAORDINARY RESULT" BUT WAS CONSISTENT WITH THE PRECEDENT OF THIS COURT AND THE DECISIONS OF THE CIRCUIT COURTS OF APPEAL

Petitioner argues that there is a conflict with *United States v. Freights etc. of the S.S. MOUNT SHASTA*, 274 U.S. 466 (1927); *Union Industrielle et Maritime v. Nimpex Int'l, Inc.*, 459 F.2d 926 (7th Cir. 1972); *The DIANA*, 423 F.2d 1 (2d Cir. 1970); *American Steel Barge Co. v. Chesapeake & O. Coal Agency Co.*, 115 F. 669 (1st Cir. 1902); and *Tagart Beaton & Co. v. James Fisher & Sons*, 1 K.B. 391 (C.A. 1903)[3]. None of these decisions, however, held that the lien on subfreights

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[3] Cornish also urges a conflict with *Beverly Hills Nat'l Bank & Trust Co. v. Compania de Navegacione Almirante S.A.*, 437 F.2d 301 (9th Cir.), *cert. denied*, 402 U.S. 996 (1971). In *Beverly Hills*, however, a claim was made for imposition of a constructive trust. No such claim was presented in this case. Indeed, as stated in note 2, *supra*, Cornish has commenced a separate action against INB while this matter was *sub judice* before the Second Circuit, urging this precise claim. Moreover, Cornish's arguments in notes 17 and 18 of the Petition are not well founded. Freight pre-paid bills of lading are not misrepresentations of the status of the freight, but an expression of the extension of credit to the recipient of the bill of lading. *See, e.g., Compania Sud Americana de Vapores v. Atlantic Caribbean Shipping Co.*, 587 F. Supp. 410 (S.D. Fla. 1984). The relationship between Ferromet and INB was a debtor-creditor relationship, not a confidential relationship. Finally, there was no competent evidence of an assumption by POSCO regarding satisfaction of Cornish's claim. To the contrary, POSCO's own letter agreement makes no reference to such a payment or use of the L/C funds.

reached a specific fund and allowed tracing of the fund into the charterer's accounts.

In this Court's decision in the *MOUNT SHASTA*, the subfreights were specifically referred to as an intangible, *i.e.*, the debt owing from the consignee to the charterer. 274 U.S. at 470. Enforcement of the lien on the debt required only that the debtor be subject to the jurisdiction of the court. This Court explained:

> Here the debtor is within the power of the Court and therefore the debt, if there is one, is also within it.

Id. at 471.

Similarly, in *American Steel Barge*, the First Circuit likened the owner's rights under the lien on subfreights to that of an assignee, 115 F. at 673, being subrogated to the remedies of the charterer, *Id.* at 674. The court explained that the action proceeds against the freight, with process to be served on "the holder of the bill of lading, or owner of the cargo, requiring him to pay the freight into the registry of the court." *Id.* at 674. Although not explicitly stated, the holder or owner are the proper parties to be notified, since they are the debtors responsible for payment of the freight.

In *Tagart, Beaton*, Lord Alverstone similarly concluded:

> [B]ut such a lien does not confer the right to follow the money paid for freight into the pockets of the person receiving it simply because that money has been received in respect of a debt which was due for freight.

1 K.B. at 395.

In *Nimpex* and *DIANA*, the courts reviewed the payment history of the freights. The *Nimpex* court found that freight payment had been made, thereby extinguishing claims by the owner. 459 F.2d at 930. This conclusion accords with the Second Circuit's analysis in the case at bar. As Chief Judge Newman explained:

> If it were true that the lien gave the owner an interest in the subfreights as funds, it would be logical for the owner to be able to execute the lien against those funds, or any identifiable portion of them, even if the consignee had paid them to the charterer before receiving notice of the lien. Under those circumstances, payment prior to notice should, at most, discharge the consignee's personal liability, rather than extinguish the owner's lien altogether. On the other hand, if the lien attaches to the subfreight only as a debt, it is easy to see why payment prior to notice completely extinguishes the lien: in that case, there is no longer any debt to attach.

(App. 13a-14a).

The comments by the *DIANA* court regarding payment similarly rest on the conclusion that the lien attaches to the subfreights as a debt, not as a separate fund. 423 F.2d at 5-6. Otherwise, the payment issue which the *DIANA* court found significant enough to require a remand for trial would actually have been immaterial.

The Second Circuit's opinion in this case harmonizes the many precedents regarding the lien on subfreights. It identifies the thread that runs through the analysis of each of these prior decisions; an analysis that in each case, explicitly or implicitly, recognizes that the lien operates on the intangible, *i.e.*, the debt which was due for freight.

Contrary to the argument of Cornish, this analysis does not undermine or obstruct enforcement of the lien. Thus, proceedings may be begun against the debtor, wherever the debtor is present either personally or through an agent. As this Court observed in *MOUNT SHASTA*, the debt is subject to arrest in these jurisdictions. This is, of course, without mention of the fact that the owner retains its right to assert its claims against the charterer or the payor.

Equally important, the Second Circuit's well-reasoned analysis preserves the limited nature of the lien, recognizing that

it exists solely to encourage commerce and shipping, not "for the assurance of the parties." *The SATURNUS*, 250 F. at 414. In view of the absence of notice, such a lien "may operate to the prejudice of prior mortgagees or of purchasers without notice." *Seaboard Fisheries*, 254 U.S. at 12. The lien is therefore strictly construed.

In summary, this case does not conflict with this Court's decision in *MOUNT SHASTA*, nor with the decisions of the other Courts of Appeal. The Second Circuit's analysis and conclusion recognizes the lien on subfreights and provides an appropriate framework for its enforcement.

CONCLUSION

RESPONDENT RESPECTFULLY SUBMITS THAT A WRIT OF CERTIORARI SHOULD NOT ISSUE TO REVIEW THE DECISION BELOW.

Respectfully submitted,

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No. 95-130

In The

Supreme Court of the United States

October Term, 1995

CORNISH SHIPPING LTD.,

Petitioner,

vs.

INTERNATIONAL NEDERLANDEN BANK N.V., f/k/a NMB POSTBANK GROEP, N.V.,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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CORNISH'S PRELIMINARY STATEMENT AND RESPONSE TO INB'S STATEMENT OF THE CASE

The thrust of INB's Brief In Opposition is designed to downplay how significant an impact the *Cornish* decision will have on the shipowning community, and otherwise convince the Court that this is just another "run of the mill" admiralty decision which should be brushed aside. Nothing could be further from the reality of the situation. In fact, what this Court has to decide is whether it is prepared to permit a major erosion of the shipowner's lien on subfreight in favor of the banking community.

Contrary to the position asserted by INB, Cornish does not seek an extension of the lien on subfreight. Similarly, Cornish does not even suggest that it should be permitted to chase the funds into the pocket of the charterer. Instead, Cornish seeks merely to reestablish the fundamental nature of its *in rem* right to proceed against the *res*.

Prior to the *Cornish* decision, the test determination of a shipowner's entitlement to subfreight was evaluated under a straightforward, almost mechanical test involving the status of the *res* at the time the shipowner exercised its lien. The *Cornish* decision changed both this test and the fundamental nature of the lien in favor of lending institutions which routinely finance these transactions. Henceforth, such land based junior lienors will be free to actively participate with impunity in the payment transaction, thereby destroying the shipowner's superior lien.

The only thing Cornish seeks from this Court is an opportunity to restore a level playing field in this aspect of admiralty law on which there is now division among the Circuits.

FURTHER REASONS FOR GRANTING THE WRIT

I.

THE LIEN ON SUBFREIGHT CAN HARDLY BE DESCRIBED AS "SECRET" AND THE ENFORCEMENT OF AN EXISTING LIEN IS NOT SUBJECT TO THE DOCTRINE OF *STRICTI JURIS.*

The shipowner's lien on subfreight can hardly be described as "secret", especially in the context of financial institutions which routinely lend on these transactions.[1] Indeed, it can hardly be described as secret to anyone even remotely familiar with ocean transportation. The lien has been recognized as far back as the last century, and has been incorporated in the standard NYPE form charter party for almost 100 years (Petition at 7).

In the case of INB, it certainly came as no surprise. INB admittedly financed numerous prior charter party transactions for Ferromet (Br. In Opp. at 2), and had specifically required that a copy of the Cornish charter party be provided to it with the Letter of Credit documents. More importantly, INB's own financing documentation with Ferromet specifically carved out an exception for these types of carrier liens.[2] As such, INB's intimation that Cornish's lien came as a surprise rings hollow, and its suggestion that this so-called secret lien operated to its prejudice flies in the face of its own financing documentation.

---

1. The reference to these types of liens being secret merely refers to the fact that recording is not a prerequisite. The same holds true for INB's assignment from Ferromet of the rights to the proceeds.

2. The security agreement between INB and Ferromet specifically excluded what was described as "permitted liens", a term defined to include liens imposed by law for carriers, materialmen, warehousemen,. . . and other like liens arising in the ordinary course of business.

Similarly, INB's repeated references to the doctrine of *stricti juris* in connection with its argument that Cornish seeks to expand its lien is misplaced (Br. In Opp. at 7). Within an established category of liens, the doctrine is generally not applied. Instead, a liberal interpretation is given to ensure effective enforcement. *See Atlantic & Gulf Stevedores v. M/V Grand Loyalty*, 608 F.2d 197, 201 (5th Cir. 1979):

> It is abundantly clear that new types of maritime liens may not be created; however, it appears equally clear that the doctrine of *stricti juris* does not affect the mechanics of the imposition of traditionally recognized varieties of maritime liens.[3]

Therefore, and in the context of Cornish's enforcement of its well recognized lien on subfreight, this Court should not apply a restrictive or narrow interpretation as to how that lien can be enforced.

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3. *See also* 2 T. Russel, *Benedict on Admiralty*, § 39 at 3-44 (1995) *citing Payne v. S.S. Tropic Breeze*, 423 F.2d 236 (1st Cir.), *cert. denied*, 400 U.S. 964 (1970), *modified on other grounds*, 456 F.2d 137 (1st Cir. 1972); 7A J. Moore, *Moore's Federal Practice*, ¶ C.07 at 660 (2d ed. 1995) ("Clearly, the 'extensions' against which the Supreme Court has long admonished were not intended to impede normal growth."); *Clubb Oil Tools, Inc. v. M/V George Vergottis*, 460 F. Supp. 835, 840 (S.D. Tex. 1978) (citing authority calling for a liberal interpretation of the term "necessaries" [an established category of liens] within the scope of the Federal Maritime Lien Act).

II.

CORNISH SEEKS NO EXPANSION OF ITS MARITIME LIEN ON SUBFREIGHT BUT ONLY ENFORCEMENT OF THAT LIEN.

INB suggests that the relief sought by Cornish would constitute an expansion of the maritime lien on subfreight. Cornish is not asking this Court to fashion a new lien or even extend the scope of its clearly recognized lien on subfreight. Cornish merely seeks enforcement of its lien against the *res* — the traditional enforcement remedy.[4]

INB's motivation in this case is clear. The *Cornish* decision significantly enhances the value of the bank's land based security interest. Further, the decision insulates the bank against criticism for manipulation of the transfer into its hands — the very basis upon which it now argues that the lien is lost. Cornish seeks only to reestablish the lien to its original status.

III.

CORNISH'S LIEN ON THE SUBFREIGHT WAS SUPERIOR TO THE BANK'S INTEREST AND REQUIRED SEGREGATION OF THE FUND UPON RECEIPT SINCE NOTICE WAS GIVEN BEFORE THE TRANSFER.

There is no dispute that INB was a competing creditor of the shipowner (Cornish) in this case (Br. In Opp. at 2). In addition, there is no dispute that Cornish's maritime lien primes the bank's interest and, in fact, prevails over *all* non-maritime security

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4. In fact, it is INB that seeks an artificial restriction of the shipowner's lien, narrowing its focus solely to an *in personam* action against the payor.

interests.[5] Finally, the shipowner's superior lien on subfreight mandates that a land based assignee "assumes the risk that his rights are subordinate to the owner's." 2 T. Russel, *Benedict on Admiralty*, § 45 at 3-70 (1995).

Despite these established principles, the Court below fashioned a new subfreight test which changed the focus of the lien. By so doing, the Court allowed the bank to retain the subfreight, despite prior service of Cornish's notice of lien and Rule C Arrest. In an effort to sustain this ruling, INB would have this Court believe that restoring the focus of the lien to the *res* itself would wreak havoc on the banks because it would supposedly enable a shipowner to chase subfreight into a charterer's account. This is not Cornish's position, Cornish does not seek such relief, and INB grossly overstates the ramifications of a restoration of the lien.

INB's obligation upon receipt of the subfreight was simple: it was obliged to segregate that fund pending further Court order regarding priority. This obligation could hardly be described as being even remotely disruptive of banking practice. Moreover, such duty will not work to the prejudice of other creditors of the charterer since the fund would be maintained in a segregated account, thereby providing notice of the shipowner's interest.

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5. *See The Lottawanna*, 87 U.S. 201, 221 (1874); G. Robinson, *Robinson On Admiralty*, §§ 60, 61 (1939); 2 T. Russell, *Benedict on Admiralty*, § 51 (1995); G. Gilmore & C. Black, *The Law of Admiralty*, at 734 (2d ed. 1975)("The two simplest propositions are that maritime claims outrank non-maritime claims. . . "); *see also In Re Topgallant Lines, Inc.*, 125 B.R. 682, 687 (Bankr. S.D. Ga. 1991) *citing The Freights of the Kate*, 63 F.707 (D.N.Y. 1894); ("It is well settled that the holder of a valid maritime lien enjoys a priority position superior to the holder of a consensual assignment for collateral purposes of an interest in freights."); *Taiwan Int'l Line Ltd. v. Matthew Ship Chartering Ltd.*, 546 F. Supp. 826, 829 (S.D.N.Y. 1982) (Shipowner's lien on subfreight prevails over prior land based security interest in proceeds of the charterer.)

In a similar vein, INB's argument that Cornish's position will have a negative impact on banking commerce is groundless. For as long as this lien has been in existence, banks have been lending money to charterers to finance ocean transportation notwithstanding the lien on subfreight. Accordingly, there is no substantive justification for the erosion of the shipowner's lien which has occurred in this case in favor of the banks.

CONCLUSION

This is the only time a bank has been able to interject itself into the subfreight payment transaction, and successfully retain those subfreights despite a prior exercise by a shipowner of its superior lien on that *res*. The *Cornish* decision's nullification of such a fundamentally important shipowner's remedy stands in stark contrast to general maritime lien law, and necessitates this Court's intervention so as to restore uniformity among the Circuits. Certiorari should be granted.

Respectfully submitted,

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